

LANESBOROUGH REIT

2008 ANNUAL REPORT



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Unitholder Returns

	Year Ended December 31, 2008	Year Ended December 31, 2007
Distribution per unit	\$0.56	\$0.56
Opening unit price	\$4.99	\$5.90
Closing unit price	\$2.30	\$4.99
Annualized yield on opening price (distribution/opening unit price)	11.2%	9.5%

Lanesborough Real Estate Investment Trust Units are listed on the Toronto Stock Exchange under the symbol "LRT.UN". The Series F and Series G convertible debentures are listed on the Toronto Stock Exchange under the symbol "LRT.DB.F" and "LRT.DB.G", respectively.

PRESIDENT'S MESSAGE

During 2008, the net operating income ("NOI") of the property portfolio of LREIT increased by \$15.0 Million, with the Fort McMurray portfolio accounting for 86% of the increase. Overall, the Fort McMurray portfolio accounted for 60% of the total NOI of LREIT during 2008. As a result of the growth in NOI, cash from operating activities increased by \$5.3 Million or 75% during 2008, compared to 2007. LREIT also achieved full distribution coverage in 2008 with distributable income exceeding distributions paid by \$1,434,465 or 14%.

A summary of the operating results of LREIT for 2008, compared to 2007, is provided in the following chart.

Financial Summary - 2008

	Year ended December 31					
	Total			Per Unit - Basic		
	2008	2007	% Change	2008	2007	\$ Change
Cash from operating activities	\$ 12,415,514	\$ 7,079,227	75 %	\$ 0.710	\$ 0.406	\$ 0.304
Distributable income	\$ 11,464,021	\$ 5,724,554	100 %	\$ 0.656	\$ 0.328	\$ 0.328
FFO	\$ 3,155,394	\$ 2,000,321	58 %	\$ 0.180	\$ 0.115	\$ 0.065
AFFO	\$ 8,053,056	\$ 2,896,707	178 %	\$ 0.461	\$ 0.166	\$ 0.295
Total revenue	\$ 66,802,294	\$ 46,311,315	44 %	\$ 3.820	\$ 2.653	\$ 1.167
NOI	\$ 42,070,145	\$ 27,072,655	55 %	\$ 2.406	\$ 1.551	\$ 0.855
Loss for the year	\$ (9,607,056)	\$ (1,400,904)	586 %	\$ (0.549)	\$ (0.080)	\$ (0.469)

The decline in oil prices, is having a negative impact on the multi-family residential rental market in Fort McMurray. As a result of the sudden weakness in rental market conditions, it is expected that LREIT may experience a reduction in cash from operating activities in 2009.

The economic uncertainty has also resulted in a more restrictive lending market. As a result of the projected reduction in operating cash flow, LREIT believes that it is prudent to reduce the amount of its annual distributions in order to lower the borrowing needs of the Trust. Specifically LREIT has established a total distribution policy of \$0.27 per unit for 2009, compared to a total of \$0.56 per unit for 2008.

The reduction in the total distribution for 2009 is being implemented with a change in the distribution policy from monthly distributions to quarterly distributions. Specifically, quarterly distributions of \$0.06 per unit (\$0.24 per unit annualized) would be payable on July 15, October 15 and December 31 to the Unitholders of record as of June 30, September 30 and December 31, respectively. The three quarterly distributions in the combined amount of \$0.18 per unit, plus the distributions of \$0.04667 per unit for January 2009 and February 2009 comprise the total projected annual distribution of \$0.27 per unit for 2009. The reduced distribution for LREIT provides Unitholders with a reasonable return, and upside potential when there is a turnaround in rental market conditions in Fort McMurray.

During 2009, the focus of LREIT will be to maximize the operating income of its property portfolio through tenant retention initiatives, value-added capital expenditures and the reduction of operating costs. LREIT will also undertake a divestiture program, for \$150 Million of assets at appraised values. The proceeds of sale will be used for the repayment of higher cost and shorter term debt of LREIT. The objective of the divestiture program is to reduce total debt, including convertible debenture debt, by a minimum of 25%, and to reduce the total debt to appraised value ratio to approximately 60%.

The consumption and price of oil will likely recover over time, leading to an eventual turnaround in the rental market in Fort McMurray. Given the relative strength and geographical diversification of the properties that are located outside of Fort McMurray, we remain optimistic regarding the future prospects of LREIT.

The Board of Trustees and the management team of Shelter Canadian Properties Limited remain fully committed to maximizing the long-term investment returns to the Unitholders.

ARNI C. THORSTEINSON, CFA
Chief Executive Officer
March 24, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

Management's Discussion and Analysis ("MD&A") of Lanesborough Real Estate Investment Trust ("LREIT" or the "Trust") should be read in conjunction with the financial statements of LREIT for the year ended December 31, 2008 and with reference to the quarterly reports for 2008.

Forward-Looking Information

Certain statements contained in this MD&A and in certain documents incorporated by reference herein are "forward-looking statements" that reflect the expectations of management regarding the future growth, results of operations, performance, prospects and opportunities of LREIT. Readers are cautioned not to place undue reliance on forward-looking information. All statements other than statements of historical fact contained or incorporated by reference herein are forward-looking statements including, without limitation, statements regarding the timing and amount of distributions and the future financial position, business strategy, potential acquisitions, plans and objectives of LREIT. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions. Such forward-looking statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements involve significant risks and uncertainties. A number of factors could cause actual results to differ materially from the results discussed in forward-looking statements including risks associated with debt financing, availability of cash for distributions, the proposed taxation of trusts, public markets, real property ownership, liquidity, interest and financing risk, credit risk, concentration of portfolio in one market, future property acquisitions, dependence on natural resources industries, reliance on single or anchor tenants, availability of suitable investments, land leases, general uninsured losses, interest rate fluctuations, Unitholder liability, potential conflicts of interest, changes in legislation and investment eligibility, conversion to international financial reporting standards, multi-family residential sector risk, environmental risks, other tax-related risk factors, supply risk, utility and property tax risk, government regulation, nature of Units, dilution, competition, general economic conditions, current economic conditions, relationship with the property manager, reliance on key personnel and additional risks associated with convertible debentures. Although the forward-looking statements contained or incorporated by reference herein are based upon what management believes to be reasonable assumptions, LREIT cannot assure investors that actual results will be consistent with these forward-looking statements.

The forward-looking statements contained herein are expressly qualified in their entirety by this cautionary statement. Forward-looking statements are made as of the date hereof, or such other date specified in such statements, and neither LREIT nor any other person assumes any obligation to update or revise such forward-looking statements to reflect new information, events or circumstances, except as expressly required by applicable securities law.

Purchase Price Information

All purchase prices set forth herein are disclosed prior to closing costs, other adjustments on closing and GST where applicable.

Appraised Value

In this management discussion and analysis, references are made to the appraised value of LREIT's property portfolio.

In summary, the total appraised value of the property portfolio is \$791,585,000 at December 31, 2008. Appraisals of 20 properties, representing 47.6% of total appraised value, were prepared in 2008, appraisals of 15 properties, representing 46.4% of total appraised value, were prepared in 2007 and appraisals of nine properties, representing 6% of total appraised value were prepared in 2006 and earlier.

The appraised value is based on appraisals prepared by independent appraisers. The appraisals are estimates only, are made effective as at the date set forth in the appraisal and are subject to a number of assumptions, qualifications and limiting conditions, including but not limited to those described in such appraisals. Such assumptions, qualifications and limiting conditions generally include, among other things: (i) that title to the property is good and marketable; (ii) there are no encroachments, encumbrances, restrictions, leases or covenants that would in any way affect valuation, except as noted in the appraisal; (iii) the existing use of the property is legal and may be continued by any purchaser of the property; (iv) there has been no delinquency in the payment of taxes relating to the property; (v) that environmental laws have been complied with and there are no potentially hazardous materials on the property or any adjoining property; and (vi) that there are no patent or latent defects in the buildings located on the property.

There can be no assurance that appraised value of a property is an accurate reflection of the value of such property as at the effective date set forth in the appraisal or on any other date, including on December 31, 2008. In addition, there can be no assurance that the valuation method or the capitalization rate(s) used in appraising a property was appropriate for such property as at the effective date set forth in the appraisal or on any other date, including on December 31, 2008.

LREIT undertakes no obligation to update the appraised value of its portfolio from time to time.

FINANCIAL AND OPERATING SUMMARY

	Year Ended December 31	
	2008	2007
DISTRIBUTIONS		
Total, including distributions on LP units	\$ 10,029,556	\$ 9,967,360
Per unit	\$ 0.56	\$ 0.56
KEY PERFORMANCE INDICATORS (1)		
Operations		
Average residential occupancy rate	95 %	95 %
Operating residential cost ratio	36 %	42 %
Operating Results		
Total revenue	\$ 66,802,294	\$ 46,311,315
Net operating income *	\$ 42,070,145	\$ 27,072,655
Income (loss) for the year before future income tax *	\$ (8,341,014)	\$ (6,133,767)
Income (loss) for the year	\$ (9,607,056)	\$ (1,400,904)
Cash Flows		
Cash flow from operating activities	\$ 12,415,514	\$ 7,079,227
Funds from Operations (FFO) *	\$ 3,155,394	\$ 2,000,321
Adjusted Funds from Operations (AFFO) *	\$ 8,053,056	\$ 2,896,707
Distributable income *	\$ 11,464,021	\$ 5,724,554
Financing		
Mortgage loans to appraised value ratio *	55 %	59 %
Weighted average interest rate of mortgage loans *	6.4 %	6.2 %
Per Unit		
Net operating income *		
- basic	\$ 2.406	\$ 1.551
- diluted	\$ 1.648	\$ 1.144
Income (loss) for the year, before future income tax*		
- basic	\$ (0.477)	\$ (0.351)
- diluted	\$ (0.477)	\$ (0.351)
Income (loss) for the year		
- basic	\$ (0.549)	\$ (0.080)
- diluted	\$ (0.549)	\$ (0.080)
Distributable income *		
- basic	\$ 0.656	\$ 0.328
- diluted	\$ 0.592	\$ 0.321
Funds from Operations (FFO) *		
- basic	\$ 0.180	\$ 0.115
- diluted	\$ 0.172	\$ 0.112
Adjusted Funds from Operations (AFFO) *		
- basic	\$ 0.461	\$ 0.166
- diluted	\$ 0.437	\$ 0.163

(1) Non-GAAP Measurements

Items marked with an asterisk represent measurements which are not calculated or presented in accordance with Canadian generally accepted accounting principles ("GAAP") or which do not have a standardized meaning as prescribed by GAAP. The non-GAAP measurements may not be comparable to the measurements which are provided by other entities and should not be used as an alternative to the measurements which are determined in accordance with GAAP for purposes of assessing the performance of LREIT. LREIT believes, however, that the non-GAAP measurements are useful in supplementing the reader's understanding of the performance of the Trust. Details regarding the calculation of the non-GAAP measurements and a reconciliation to GAAP measurements, where applicable, are provided in the report.

EXECUTIVE SUMMARY

Business Strategy

The primary objectives of the Lanesborough Real Estate Investment Trust ("LREIT" or the "Trust") are to maximize unit values and provide stable cash distributions to the Unitholders by creating a large diversified portfolio of quality real estate investments through the ongoing acquisition and development of multi-unit residential properties.

During the past three years, LREIT has focused its investment activities on the acquisition and development of new residential rental properties in Fort McMurray, Alberta due to the high level of economic growth in Fort McMurray and the favourable rate of return generated by real estate investments in the City.

Acquisition and Development

During 2008, LREIT completed the construction and development of Laird's Landing in Fort McMurray, acquired Siena Aaprtments, a residential property in Fort McMurray, acquired possession under an agreement to purchase of Parsons Landing, a residential property in Fort McMurray, and acquired Colony Square in Winnipeg, Manitoba. As of December 31, 2008, the property portfolio of LREIT consists of 40 residential properties and four commercial properties, with a total purchase price of approximately \$597 Million, encompassing 3,913 suites and 307,735 square feet of leasable area.

As disclosed in greater detail in this report, the purchase agreement for Parsons Landing provided for the payment of the balance amount owing to be made in February 2009. As a result of a delay in funding the mortgage loan financing for the property, the payment of the balance owing has also been delayed until the second quarter. (See "Parsons Landing" on page 13.)

Cash from Operating Activities and Net Operating Income ("NOI")

During 2008, LREIT generated cash from operating activities of \$12.4 Million, representing an increase of \$5.3 Million or 75%, compared to 2007. The increase in cash from operating activities mainly reflects an increase in the NOI of the residential property portfolio, partially offset by an increase in the cash component of financing expense.

During 2008, the NOI from the portfolio of residential properties increased by \$15.0 Million or 55%, while the cash component of financing expense increased by \$8.8 Million or 46%. The increase in NOI is mainly attributable to the new income-producing properties in Fort McMurray. In total, the new income-producing properties in Fort McMurray accounted for 40.6% of increase in NOI during 2008.

The increase in the cash component of financing expense is almost entirely attributable to an increase in interest expense on mortgage loans payable. During 2008, mortgage loan debt increased by approximately \$112.6 Million, of which approximately 78% pertains to longer term financing for specific income properties and approximately 22% pertains to short-term interim mortgage financing.

The increase in cash from operating activities is also reflected in the increase in distributable income. During 2008, distributable income increased by \$5.7 Million or 100% and LREIT achieved a distribution coverage ratio for distributable income equal to 1.14 and a coverage ratio based on cash from operating activities of 1.24.

Loss for the Year

During 2008, the net loss of LREIT was \$9.6 Million, compared to a loss of \$1.4 Million in 2007. The variance between the 2008 and 2007 loss, as well as the variance between the 2008 loss and the 2008 cash flow of \$12.4 Million is mainly attributable to three non-cash components of the financial results:

- during 2008, LREIT recorded an unrealized book loss of \$4 Million as a result of a change in the carrying value of the interest rate swap arrangements between the time that the swap arrangements were implemented in 2008 and the end of the year. The change in value is reflected as a charge to financing expense and is subject to adjustment based on changes in interest rates in the future;
- amortization charges increased by \$3.2 Million in 2008, mainly due to the increase in the cost base of income properties; and
- the amount of the future income tax expense (recovery) changed by \$6 Million in 2008, compared to 2007. The income tax expense serves to increase the loss of the Trust.

In very general terms, the future income tax expense (recovery) reflects the change in the net tax position of the Trust in 2008, after accounting for future income tax assets and liabilities associated with the wholly-owned subsidiaries of the Trust and the potential change in the tax status of the Trust in 2011, net of current taxes payable.

The change to a future income tax expense in 2008 from a future income tax recovery in 2007 is mainly due to the valuation allowance recorded in regard to the future income tax asset relating to the operating losses of the wholly owned subsidiaries in 2008. The future income tax recovery was comparatively high in 2007, as the future income tax assets and liabilities associated with the potential change in the tax status of the Trust, in the net asset amount of approximately \$3.8 Million, were initially recorded in 2007.

Outlook for 2009

The downturn in the multi-family residential rental market in Fort McMurray in 2009 has negatively impacted the cash flow projections of the Trust. Although it is difficult to predict the length of the economic slowdown in Fort McMurray, it is anticipated that there may be a decrease in cash from operating activities during 2009.

Given the projected decrease in cash flow, and to minimize the extent of any additional interim financing, it is necessary for LREIT to reduce the amount of its annual distribution. Specifically, the distribution policy of LREIT is being reduced from monthly payments of \$0.04667 per unit (\$0.56 annually) to quarterly payments of \$0.06 per unit (\$0.24 annually). The first quarterly distribution will be paid on July 15, 2009, for the three month period ending June 30, 2009. After considering the distribution which was declared for January and February 2009, the total distribution for 2009 is projected to be \$0.27 per unit. A distribution will not be declared for March 2009.

From a longer term perspective, management believes that the cash flow results for the fourth quarter of 2008 reflect the cash flow generating potential of the property portfolio. During the fourth quarter of 2008, cash from operating activities amounted to \$5,761,651 or \$23,046,604 on an annualized basis, representing an amount which is sufficient to fully fund the total regular monthly mortgage loan principal payments, property improvement costs and cash distributions which were incurred in 2008.

OVERVIEW OF OPERATIONS AND INVESTMENT STRATEGY

General

Lanesborough Real Estate Investment Trust ("LREIT") is an unincorporated closed-end real estate trust which was established on April 23, 2002, under the laws of the Province of Manitoba. LREIT became a publicly traded entity on August 30, 2002. The trust units of LREIT are listed on the Toronto Stock Exchange under the symbol "LRT.UN" and the Series F and Series G convertible debentures are listed on the Toronto Stock Exchange under the symbol "LRT.DB.F" and "LRT.DB.G", respectively.

The investment policies and operations of LREIT are subject to the overall control and direction of the Trustees, pursuant to the terms of the Declaration of Trust. Shelter Canadian Properties Limited ("Shelter Canadian") provides asset management services to LREIT, pursuant to the terms of a Services Agreement. Shelter Canadian is also responsible for the property management function for the income properties of LREIT, pursuant to the terms of a Property Management Agreement.

The primary business activity of LREIT is the acquisition and development of income-producing real estate properties and the active management of the acquired/developed properties. Aside from four commercial properties which were acquired by LREIT in the initial years of operation, the real estate portfolio of LREIT consists entirely of multi-family residential rental properties. Rental revenue from the leasing of the residential suites is the primary source of revenue for LREIT. The income properties are located in rental markets across western Canada and in Ontario and the Northwest Territories.

The financial statements of LREIT provide segmented results for the income properties by geographic location and by property type. Operating results pertaining to general Trust operations are disclosed separately in the segmented financial information.

Investment in Properties

The general investment strategy of LREIT has been to create a geographically diversified portfolio of rental properties, offering strong growth potential, with an emphasis on investments in smaller cities across western Canada. During the past 2 ½ years, LREIT has focused its investment activities on the acquisition and development of new residential rental properties in Fort McMurray, Alberta due to the high level of economic growth in Fort McMurray and the favourable rate of return generated by real estate investments in the City in recent years.

The new income-producing properties which were acquired or developed by LREIT in Fort McMurray during 2007 and 2008 are primarily responsible for the significant growth in operating income and operating cash flow that was achieved by LREIT in 2008.

Operations

LREIT strives to maximize the operating income of its property portfolio through the implementation of sophisticated and prudent financial management practices, superior operating procedures, high calibre and responsive management services and proactive leasing strategies. LREIT also completes capital improvements and upgrades to its properties on an ongoing basis and undertakes major renovation programs or expansion projects at selected properties, as deemed appropriate.

The most comprehensive renovation program or expansion projects have occurred at two properties (Elgin Lodge and Highland Tower) and less extensive renovation programs have been completed at several other properties.

Occupancy levels and profit margins for the portfolio of "same" properties are key indicators which are used by LREIT to assess the impact of property improvements and the overall performance of properties which have been in the income-producing stage for at least 24 consecutive months. During 2008, the portfolio of same residential properties achieved an average occupancy level of 95% and a profit margin of 56%, compared to 95% and 55%, respectively, in 2007.

Financing

The purchase price of new property acquisitions is typically funded from the proceeds of mortgage loan financing with the remaining balance, or the equity component, funded from reserves of investment capital (i.e., cash). The investment capital of LREIT has been primarily raised through the completion of trust unit or convertible debenture offerings, although LREIT also utilizes interim mortgage loans, bridge financing and an operating line of credit as a source of investment capital. The upward refinancing of mortgage loan debt has also served as a source of investment capital.

Pursuant to the terms of the Declaration of Trust, the total mortgage indebtedness of LREIT shall not exceed 75% of the appraised value of LREIT's property portfolio. As of December 31, 2008, the total mortgage indebtedness of LREIT is equal to 64% of the appraised value of the property portfolio.

The ratio of net operating income, to mortgage loan debt service costs, is one of the variables which is used by LREIT to assess the overall financial position of the Trust. During 2008, the mortgage loan debt service coverage ratio was 1.3, compared to 1.1 in 2007.

Current Economic Conditions

There is currently a high level of economic uncertainty and financial market volatility throughout the global marketplace. The operations and business strategies of LREIT are discussed in additional detail in the following section of this report, with specific regard to the impact of the current economic conditions.

IMPACT OF ECONOMIC AND FINANCIAL UNCERTAINTY ON OPERATIONS

General Considerations

Time-Line

The collapse of global financial markets was essentially triggered in the fourth quarter of 2008, as ongoing news of the severity of the financial crisis intensified and stock markets throughout the world experienced historic declines in value.

The events which led to the decline of global financial markets also created a heightened level of economic uncertainty and a more restrictive and conservative mortgage lending market. The economic and financial uncertainty has also affected the overall operations and business strategies of LREIT.

Reduction of Distributions

As a result of the continuing deterioration of the Canadian economy, it is anticipated that there will be a significant reduction in the operating cash flow of LREIT during 2009 and a corresponding reduction in the amount of cash which is available to fund distributions. Given the degree of uncertainty which exists in regard to projected cash flow amounts, LREIT also believes that it is prudent to take a conservative approach in establishing the level of distributions for 2009. In this regard, LREIT has established a total distribution of \$0.27 per unit for 2009, compared to a total of \$0.56 per unit for 2008.

The reduction in the total distribution for 2009 is being implemented in conjunction with a change in the distribution policy from monthly distributions to quarterly distributions, effective immediately. Specifically, LREIT is implementing a change from a monthly distribution policy to a quarterly distribution policy, whereby quarterly distributions of \$0.06 per unit (\$0.24 per unit annualized) would be payable on July 15, October 15 and December 31 to the Unitholders of record as of June 30, September 30 and December 31, respectively. The three quarterly distributions in the combined amount of \$0.18 per unit, plus the distributions of \$0.04667 per unit for January 2009 and February 2009 comprise the total projected distribution of \$0.27 per unit in 2009. A distribution will not be paid in April 2009.

Unit Value

Although there are a multitude of complex factors affecting the price of a publicly traded investment, the volatility in global stock markets has negatively impacted the trading price of the trust units of LREIT, since the second quarter of 2008 when the price of oil peaked. The impact of ongoing economic and financial uncertainty on financial markets continues to be one of the primary risk factors associated with publicly-traded investments, including investments in the units of LREIT.

Market Conditions

LREIT operates primarily in the multi-family residential market with the majority of residential rental revenue being generated from properties located in Alberta, Manitoba, Saskatchewan and the Northwest Territories. The highest concentration of properties is located in Fort McMurray, Alberta. During 2008, the multi-family residential rental property portfolio in Fort McMurray accounted for 60% of the total operating income of LREIT.

Global recessionary influences have impacted certain regions of Canada to a greater extent than others, with the manufacturing based economies in southern Ontario and Quebec experiencing the most significant economic slowdown, followed by commodity based economies in British Columbia and Alberta. As a result of the decline in oil prices, there has been a slowdown of economic growth in Fort McMurray and a reduction in the level of activity in the oil sands construction industry and a weakening of rental market conditions. The decline in rental market conditions is impacting the occupancy levels of LREIT's property portfolio in Fort McMurray and affecting the leasing of vacant suites and the retention of existing tenants. During the first quarter of 2009, the vacancy rate for the entire Fort McMurray portfolio is projected to be 14%, compared to 2% in the fourth quarter of 2008.

The possibility of tenants defaulting on lease agreements has also increased as a result of the decline in rental market conditions in Fort McMurray portfolio, for both individual tenancies and corporate tenants. Employees from the oil sands industry represent the primary tenant base of the Fort McMurray portfolio, however, LREIT has also two properties, encompassing a total of 241 suites, which are 100% leased to major oil sands companies under multi-year net lease agreements, expiring in 2010 and 2012, respectively.

During 2008, residential properties in Saskatchewan and Yellowknife accounted for 18% and 9% of the total rental revenues of LREIT, respectively. The contribution from the Manitoba portfolio is expected to increase significantly during 2009 as a result of the acquisition of Colony Square in October 2008.

Rental market conditions in Saskatchewan and Manitoba, as well as in Yellowknife, have not changed significantly during 2009, as the local economies are more diversified and less susceptible to the specific economic factors which are driving the recession. During the fourth quarter of 2008 and into the months of January and February 2009, the three rental properties in Yellowknife have maintained occupancy levels in excess of 98%; while the overall occupancy level for the Saskatchewan property portfolio has remained relatively stable, in large part due to the fact that the two largest properties, in terms of acquisition cost, are seniors residences which are operating at full, or near full, capacity. Similarly, the overall occupancy level for the four properties in the Manitoba portfolio has remained in excess of 95% since October 2008, including Colony Square, which has maintained an occupancy level of approximately 98% since the date of acquisition.

In the other Alberta communities where LREIT properties are located (Edmonton, Peace River and Edson), there has not been a significant change in the overall occupancy level during the last quarter of 2008 or in the first quarter of 2009. Excluding properties in Fort McMurray, the Alberta portfolio accounted for 18% of the total revenues of LREIT during 2008.

In summary, the weaker rental market in Fort McMurray is the primary economic issue facing LREIT in 2009 due to the high concentration of properties in the City. The potential impact of a prolonged period of low oil prices on the Fort McMurray rental market is one of the main risk factors for LREIT.

Although it is not possible to predict the extent to which recessionary influences will ultimately affect individual communities, management of LREIT does not expect rental market conditions in the other geographic areas where LREIT properties are located to change significantly in 2009.

Parsons Landing Transaction

Although there has been a delay in the funding mortgage loan financing for Parsons Landing, management anticipates that mortgage loan financing for Parsons Landing will be completed in the second quarter of 2009. Nevertheless, there is a risk that financing arrangements for Parsons Landing will not be completed within a satisfactory time frame and that the property will be listed for sale by the vendor (see "Parsons Landing" on page 13 for additional details).

Liquidity

Debt Maturities

The negative impact of the financial crisis on debt markets, combined with the utilization of interim sources of mortgage financing by LREIT, has also increased the level of risk for LREIT in regard to debt financing.

As disclosed in more detail in the MD&A, LREIT has \$65 Million of mortgage loan debt maturing during 2009, representing 18.5% of its total long-term debt, as of December 31, 2008. The maturing debt includes \$25 Million of interest-only mortgage loans with a term of one year. The economic and financial uncertainty has resulted in a more restrictive and conservative lending market and, in the event that LREIT is unable to renew its mortgage loan debt at maturity, or obtain replacement financing, LREIT would not be in a position to repay the debt and would be in default of its debt obligations. In such event, the lenders could potentially take action against LREIT and the indebted properties. It could also be necessary for LREIT to direct funds, which would otherwise be used for distributions, to retire mortgage debt.

In summary, the increased uncertainty in the capital markets has increased the risk of potential mortgage arrears by LREIT and could potentially affect the ability of LREIT to maintain quarterly distributions at the reduced level of \$0.06 per unit. Renewal terms have been finalized for all mortgage loans which mature in the first half of 2009 with exception of two mortgage loans with a combined principal balance of \$6.6 Million that have been extended on a short-term basis pending the completion of alternate financing arrangements. Demand loans totalling \$92,935,570 include loans of \$12,935,970, \$5.5 Million, \$18 Million and \$55 Million maturing on January 1, 2010, February 1, 2010, October 31, 2010 and November 1, 2011 respectively, as well as a loan in the amount of \$1.6 Million. Management anticipates that all mortgages maturing in 2009 will be renewed or refinanced.

Sources of Capital

In 2008 and prior years, LREIT has utilized interim sources of financing to supplement the funding of distributions, as well as the funding of income property improvements and unit repurchases under the normal course issuer bid.

In 2009, it is anticipated that the extent of additional interim financing will be minimal, as the operating cash flow of LREIT, net of mortgage loan principal payments, is expected to increase to a level which is sufficient to fully fund income property improvements, distributions, at the reduced level, and repurchases under the normal course issuer bid. In the event that occupancy levels for the property portfolio in Fort McMurray do not stabilize at acceptable levels in the upcoming months, the expected increase in operating cash flow will likely not be achieved and it will be necessary for LREIT to pursue additional interim financing as a source of capital, or implement an additional reduction in the amount of quarterly distributions.

Management of LREIT does not believe that the ability of LREIT to successfully complete additional interim financing arrangements has been significantly impaired by the current level of economic uncertainty in Canada, however, there are no assurances that this will continue to be the case for the foreseeable future. In the event that adequate interim financing arrangements can not be completed, it may be necessary for LREIT to reduce or terminate unit repurchases and/or reduce the extent of income property improvements and/or further reduce the level of distributions.

Other Risk Factors

There are many other risk factors associated with an investment in LREIT, many of which are not directly related to, or directly affected by, the current level of uncertainty in global economic conditions. As with previous reports, the key risk factors, including the above noted risks regarding public market investments, general economic conditions and the concentration of properties in Fort McMurray, are also discussed in the latter sections of the MD&A. Other risks and uncertainties are more fully explained in the other regularly filings of LREIT, including the Annual Information Form. A discussion of risk management and the management of capital is contained in the accompanying financial statements.

REAL ESTATE PORTFOLIO

Investment in Properties - 2008

Portfolio Summary - December 31, 2008

As of December 31, 2008, the property portfolio of LREIT consists of 40 residential properties and four commercial properties, with a total purchase price of approximately \$597 Million, encompassing 3,913 suites and 307,735 square feet of leasable area. One of the residential properties includes a seven-storey office building.

A list of all of the properties in the LREIT investment portfolio is provided in Schedule I of this report.

Property Acquisitions

During 2008, LREIT acquired ownership or possession over three new properties, as follows:

Siena Apartments

On July 2, 2008, LREIT acquired 66 condominium units in Fort McMurray, Alberta, in a residential complex known as Siena Apartments. The units are contained on the second, third and fourth floors of the complex and consist of six one-bedroom and 60 two-bedroom suites. All of the suites are fully furnished and the complex includes a 93 stall underground parkade. The main floor commercial condominium units are owned by a third party.

The 66 condominium units are 100% leased to a major oil sands operating company on a net rent basis until May 1, 2012. The lease agreement provides the tenant with an option to extend the lease in 2012 for an additional five years at the current market rents at that time.

The purchase price of \$30 Million was funded by a new first mortgage loan in the amount of \$21 Million, a vendor take-back mortgage loan of \$4 Million and the balance in cash. The first mortgage loan is a five year, floating interest rate mortgage, however, the interest rate has been fixed at 5.7% through an interest rate swap arrangement. The vendor take-back mortgage loan is a 5% "interest-only" mortgage with a due date of July 2, 2010.

LREIT also has a right of first refusal to acquire Cortona Apartments (formerly known as Phase II of Siena Apartments). Cortona consists of 57 suites and is also 100% leased to the same major oil sands operating company on a net rent basis for a five-year term until 2013.

Parsons Landing

On September 1, 2008, the construction of Parsons Landing was completed. Parsons Landing is a new apartment property in the Timberlea area of Fort McMurray, Alberta. The property consists of a four-storey apartment building, with a total of 160 suites, comprised of 32 one-bedroom, 124 two-bedroom and four three-bedroom suites. The majority of the suites are fully furnished and each suite has individual condominium title. The property also has a 219 stall parkade and 37 surface parking stalls.

The completion of Parsons Landing occurred in two phases upon the issuance of occupancy certificates. LREIT acquired possession of Phase I on May 14, 2008 and possession of Phase II effective September 1, 2008.

The purchase price of Parsons Landing was \$63.2 Million, including GST. The purchase agreement for Parsons Landing provided for a portion of the purchase price to be paid by February 28, 2009. After accounting for the initial deposit and a portion of the \$10 Million second mortgage loan advance that was provided to the Vendor in November 2007, the balance owing subsequent to the acquisition of Phase I was approximately \$25.3 Million, including GST. Upon the closing of Phase II, the balance owing increased to approximately \$50.7 Million, including GST. After accounting for the payment of an additional deposit of \$2.5 Million on October 1, 2008, the balance owing on Parsons Landing was \$48.2 Million as of December 31, 2008, including GST.

The funding of the mortgage financing for the property has been delayed and, as a result, the vendor has agreed to extend the deadline for payment of the balance owing until May 29, 2009 and to accept partial payment on account of interest of \$600,000, payable in two installments of \$300,000 in March and April of 2009. The payment extension is conditional upon LREIT obtaining a commitment for mortgage financing of \$45,000,000 by April 15, 2009. In the event that a financing commitment is not received by April 15, 2009, the vendor shall be permitted to list the property for sale. Depending on the price, the sale may result in the \$15,000,000 paid to the vendor to date, or a portion thereof, being lost.

Colony Square

Prior to October 1, 2008, LREIT owned a 1.5% beneficial interest in Colony Square, an apartment/office complex in downtown Winnipeg, Manitoba. On October 1, 2008, LREIT acquired the remaining 98.5% beneficial interest in the property for a total purchase price of \$37.8 Million.

Colony Square consists of two apartment towers (one with 16 storeys and one with 17 storeys), a seven storey office building and a 270 stall underground parkade. The two apartment towers contain a total of 428 suites, while the office building contains 80,935 square feet of leasable area. An additional 2,255 square feet of leasable commercial area is available on the main floor of the apartment towers.

The acquisition of Colony Square was funded by the assumption of a \$20.9 Million, 5.5% first mortgage loan and the balance of approximately \$17.2 Million from the proceeds of interim mortgage loans on existing LREIT properties.

New Income-Producing Properties

In most cases, an existing property which is acquired by LREIT is classified as an "Income Property" on the property acquisition date. Building additions and properties which are under development by LREIT, as well as newly constructed properties acquired by LREIT, are classified as "Properties Under Development" until the lease-up stage for the property is completed, or a pre-determined time period is reached, at which point the property is reclassified as an "Income Property". Construction costs and/or carrying costs of a property under development are capitalized and a property does not contribute to the operating income of the Trust until the property is reclassified as an income property.

The date on which a property becomes an "income-producing" property is, therefore, a major factor in terms of analyzing the impact of the overall growth of the property portfolio on the operating income of the Trust. During 2008, the three new properties were added to the "income-producing" portfolio of LREIT, as well as one property which was developed by LREIT, over a 21 month period, and leased up in the second quarter of 2008 (Laird's Landing). A summary of the new income-producing properties is provided in the following chart.

Property	Price	Classified as an income property	Contribution to Operating Income (In Days)
Laird's Landing	\$ 51,350,000	June 1, 2008	214
Parsons Landing Phase I	33,054,000	July 1, 2008	184
Siena	30,000,000	July 2, 2008	183
Parsons Landing Phase II	27,679,000	September 1, 2008	122
Colony Square	37,839,300	October 1, 2008	92
	<u>\$ 179,922,300</u>		

Properties Under Development

The property portfolio of LREIT includes two properties which are classified as "Properties Under Development", namely the Clarington Seniors Residence and the multi-level building addition at Elgin Lodge. The Clarington Seniors Residence was acquired by LREIT in 2007, in the lease-up stage of development, while the building addition at Elgin Lodge was completed during the fourth quarter of 2007.

Both properties will be reclassified as "income-producing" properties in 2009.

Mortgage Loan Receivable

December 31, 2008	nil
December 31, 2007	\$ 10,000,000

As of December 31, 2007, "Mortgage Loan Receivable" consisted of the \$10 Million second mortgage loan which was provided in regard to the construction of Parsons Landing. During 2008, the loan was fully applied to the purchase price of the property. As a result, the Trust did not have any investments in mortgage loans, as of December 31, 2008.

CAPITAL STRUCTURE

Capital Structure - December 31, 2008

	December 31, 2008		December 31, 2007	
	Amount	%	Amount	%
Mortgage loans payable - principal amount	\$ 456,192,133	89.9 %	\$ 343,269,160	86.6 %
Convertible debentures - face value	51,362,000	10.1 %	52,955,000	13.4 %
Trust units (net of issue costs)	79,750,666	15.7 %	79,124,607	20.1 %
Total capitalization	<u>\$ 587,304,799</u>	<u>115.7 %</u>	<u>\$ 475,348,767</u>	<u>120.1 %</u>

Trust Units

Units Outstanding

Authorized	unlimited
Issued as of,	
- December 31, 2008	17,588,081
- March 24, 2009	17,537,150

As of December 31, 2008, LREIT had 17,588,081 units outstanding, representing an increase of 58,187 units or 0.3%, compared to the number of units outstanding as of December 31, 2007. The increase in units originated from the following transactions:

<u>Issue Date</u>	<u>Units Issued</u>	<u>Equity Raised</u>
Units outstanding, December 31, 2007	17,529,894	\$ 66,457,466
Units issued under DRIP	514,387	1,802,126
Units purchased and cancelled under normal course issuer bid	<u>(456,200)</u>	<u>(1,778,440)</u>
Units outstanding, December 31, 2008	<u>17,588,081</u>	<u>\$ 66,481,152</u>

Distribution Reinvestment Plan ("DRIP")

The "Distribution Reinvestment Plan" provides that Unitholders may choose to have monthly cash distributions automatically reinvested in additional units, while receiving a "bonus" distribution of units equal to 4% of the reinvested amount. Participants in the DRIP may also purchase additional units on a distribution payment date. The purchase price of the units will generally be equal to the weighted average closing price of the units for the five trading days immediately preceding the relevant distribution payment date.

As noted above, 514,387 units were issued under the Distribution Reinvestment Plan during 2008, at an average purchase price of \$3.37 per unit, representing a total value of \$1,733,097. The value of the DRIP units is included in the determination of the total amount of distributions declared by LREIT.

Normal Course Issuer Bid

In January 2008, LREIT initiated a normal course issuer bid ("NCIB") for its trust units, under which it is entitled to purchase a limited number of the issued and outstanding units of the Trust, as specified by the TSX. The initial 12 month term of the NCIB was renewed in January 2009 for an additional 12 month term that expires on January 22, 2010.

During 2008, LREIT purchased and cancelled 456,200 units under the normal course issuer bid at a weighted average price of \$3.90 per unit. During the period from January 1, 2009 to January 30, 2009, the Trust purchased and cancelled an additional 99,507 units at a weighted average price of \$2.77, pursuant to the normal course issue bid.

LREIT believes that the ongoing purchase of units, pursuant to the bid, is an appropriate use of LREIT's resources, given management's belief that there is a disparity between the market price of the units and the underlying value of the units. LREIT also believes that the purchase of units pursuant to the bid will benefit all remaining Unitholders by increasing their proportionate equity interest and voting interest in LREIT, while affording liquidity to anyone who desires to sell their units.

LREIT will limit the number of units purchased under the NCIB during the remainder of 2009.

Unit Options

Pursuant to the Unit Option Plan, the Trust may grant unit purchase options to the Trustees, Directors and Senior Officers of LREIT and to other individuals who are employed or retained by the Trust to perform specific duties.

On January 7, 2008, LREIT granted options to acquire a total of 370,000 units to 26 individuals, including 245,000 units which were granted to the four independent trustees, the Chief Executive Officer and the Chief Financial Officer of LREIT, and 125,000 units which were granted to 20 management and other senior employees of Shelter Canadian Properties who are engaged in LREIT related functions. The options which were issued to the four independent trustees vested immediately, while the remaining options vest equally on each of the grant date and the four subsequent anniversaries of the grant date. All of the options are exercisable at a price of \$5.10.

As of December 31, 2008, LREIT had 1,452,000 options outstanding.

In accordance with Canadian generally accepted accounting principles, the estimated fair value of the options is expensed over the vesting period of the options and the expense is recorded as "unit-based compensation". Unit-based compensation expense is included in trust expense in the Consolidated Statements of Loss and Comprehensive Loss. During 2008, unit-based compensation expense related to the unit options amounted to \$391,517, including \$177,930 relating to the 370,000 units which were issued in January 2008.

As unit-based compensation is a "non-cash" expense, it does not impact the operating cash flows of the Trust.

Limited Partnership Units

In June 2006, LREIT acquired the Village West Townhouses in Saskatoon, Saskatchewan. The acquisition of the property encompassed the issuance of 456,617 Class B Limited Partnership Units ("LPU's") of a wholly owned Limited Partnership which was established by the Trust (the LREIT Village West Limited Partnership). The LPU's were issued at a value of \$6 per LPU, representing total consideration of \$2,739,704. Each LPU is entitled to receive cash distributions equal to the cash distributions which are paid on the trust units of LREIT. The vendor has the right to exchange each LPU for LREIT trust units on a one for one basis. The LPU's are also transferable.

On November 1, 2006, 100,000 of the LPU's were exchanged for LREIT trust units.

During 2008, distributions in regard to the LPU's amounted to \$199,705. The LPU distributions are included in the calculation of the "total distributions" of LREIT for purposes of analyzing the distribution payout ratio of the Trust. The distributions on the Limited Partnership units serve to reduce the "non-controlling interest" of the Village West Limited Partnership.

Deferred Unit Plan

On June 18, 2008, the Trust adopted a deferred unit plan, under which, any trustee, officer, employee, or consultant employee of the Trust may elect to have their annual bonus, annual board retainer or board meeting fees paid in the form of deferred units. Deferred units granted to Trustees shall vest immediately. Deferred units granted to participants other than Trustees shall vest 33% on the first anniversary of grant, 33% on the second anniversary of grant, and 34% on the third anniversary of grant. In the event of any change of control (as defined in the deferred unit plan), any unvested deferred units shall vest upon the earlier of the next applicable vesting date that is immediately prior to the date on which the change of control occurs. Whenever cash distributions are paid, additional deferred units are credited to the participant based on the number of deferred units held. The deferred units credited to a participant vest immediately and are redeemable by the participant on retirement or on "termination" other than for cause. If a participant is terminated for cause, only the deferred units which have vested shall be redeemable and any unvested deferred units shall be cancelled. Additional details of the Deferred Unit Plan are disclosed in note 17 to the 2008 financial statements of LREIT.

Effective July 1, 2008, the Trustees also approved a compensation package, whereby specific fees were established for the independent Trustees for serving on the Board, acting as a Committee Chair and attending meetings. During 2008, the total fees payable to independent Trustees under the compensation package amounted to \$78,787.

All of the independent Trustees elected to have their compensation for 2008 paid in the form of deferred units. The number of deferred units received is determined by dividing the amount of the compensation by the market value of the trust units, as of the date on which the compensation is payable. Based on an average market value of \$3.34, there were 23,528 deferred units granted to be independent Trustees during 2008.

The value of the deferred units is a unit-based compensation expense, including in "Trust expense" in the financial statements of LREIT. Unit-based compensation expense is a "non-cash" expense, which does not affect the cash flow of the Trust.

Distribution Dates and Amounts

During 2008, LREIT declared monthly distributions of \$0.04667 per unit, representing an annual distribution of \$0.56 per unit. Distributions in 2008 are comprised of the following components:

	<u>Trust Units</u>	<u>LP Units</u>	<u>Total</u>
Cash distributions paid for January to December, 2008	\$ 8,104,253	\$ 199,705	\$ 8,303,958
Value of units issued under DRIP	<u>1,725,598</u>	<u>-</u>	<u>1,725,598</u>
Distributions declared, per Statement of Equity	<u>\$ 9,829,851</u>	<u>\$ 199,705</u>	<u>\$ 10,029,556</u>

A cash distribution of \$0.04667 per unit was paid for the months of January and February 2009. The February 2009 distribution was paid on March 13, 2009.

As previously disclosed, LREIT is changing to a quarterly distribution policy at the reduced amount of \$0.06 per unit or \$0.24 per unit on an annualized basis. The distribution for each quarter, excluding the fourth quarter ending December 31st, is paid on or about the 15th day of the month following the quarter end, to the Unitholders of record on each quarter end. The distribution for the fourth quarter is paid on or before December 31st to the Unitholders of record on or about December 15th. Accordingly, the distribution for the second quarter of 2009 will be paid on or about the 15th day of July 2009.

As a result of the change to a quarterly distribution policy, a distribution will not be declared for March 2009.

Convertible Debentures

The Declaration of Trust for LREIT does not impose any limitations on the amount of convertible debt which may be issued by the Trust. The following is a summary of the debenture offerings which have been undertaken by LREIT, as of December 31, 2008.

Summary of Debenture Offerings

Issue Date/Maturity Date	Series	Interest Rate	Amount Issued	Repayments/Unit Conversions		Net Amount Outstanding December 31, 2008
				Year Ended December 31, 2008	As of December 31, 2007	
Aug. 30/02/Aug. 30/07	A	10.0 %	\$ 3,000,000	\$ -	\$ (3,000,000)	\$ -
Aug. 30/02/Aug. 30/05	B	8.0 %	1,000,000	-	(1,000,000)	-
Jan. 30/04/Jan. 30/06	C	8.0 %	10,131,000	-	(10,131,000)	-
Mar. 16/04/Mar. 16/08	D	8.0 %	4,000,000	(1,593,000)	(2,407,000)	-
Feb. 17/05/Feb. 17/10	E	8.0 %	12,000,000	-	(50,000)	11,950,000
Mar. 10/06/Mar. 11/11	F	7.5 %	13,680,000	-	-	13,680,000
Dec. 8/06/Dec. 31/11	G	7.5 %	25,732,000	-	-	25,732,000
Face value			<u>\$ 69,543,000</u>	<u>\$ (1,593,000)</u>	<u>\$ (16,588,000)</u>	51,362,000
Net accumulated accretion						5,833,034
Unamortized transaction costs						<u>(1,662,431)</u>
Book value, December 31, 2008						<u>\$ 55,532,603</u>
<u>Allocation of book value</u>						
Debt component						\$ 44,090,397
Equity component						13,104,637
Unamortized transaction costs						<u>(1,662,431)</u>
						<u>\$ 55,532,603</u>

The series E and F debentures provide for the outstanding amount of the debentures to become payable on demand upon default, under certain terms and conditions, of a mortgage loan or a convertible debenture. The Trust is in compliance with all covenants in regard to mortgage loans and convertible debentures as at December 31, 2008.

Mortgage Loans Payable

December 31, 2008	\$453,927,161
December 31, 2007	\$341,334,043

Summary of Mortgage Loans Payable

Year of Maturity	Weighted Average Interest Rate	Amount December 31, 2008	Percentage of Total
Fixed rate			
2009 *	7.9 %	\$ 65,044,518	14.3 %
2010	8.1 %	37,325,492	8.2 %
2011	8.5 %	7,219,058	1.6 %
2012	5.6 %	33,572,267	7.3 %
2013	5.8 %	45,883,870	10.1 %
2014	6.3 %	43,423,058	9.5 %
2015	5.6 %	57,058,516	12.5 %
2016	5.2 %	45,406,582	10.0 %
2017	5.7 %	5,746,946	1.2 %
2018	5.8 %	<u>22,576,256</u>	<u>4.9 %</u>
		363,256,563	79.6 %
Demand/floating rate	5.9 %	<u>92,935,570</u>	<u>20.4 %</u>
Principal amount		456,192,133	<u>100.0 %</u>
Difference between contractual and market interest rates on mortgage loans assumed		110,798	
Unamortized transaction costs		<u>(2,375,770)</u>	
		<u>\$ 453,927,161</u>	
<u>Principal amount:</u>			
Income properties		\$ 432,386,563	
Properties under development		<u>23,805,570</u>	
		<u>\$ 456,192,133</u>	

* Includes floating interest rate mortgage of \$22,576,256 and \$20,763,272, with interest rates fixed at 5.82% and 5.74% respectively by use of interest rate swap arrangements.

During 2008, the balance of mortgage loans payable increased by \$112,593,118, comprised of the following amounts:

	Year Ended December 31, 2008
Mortgage loans on existing properties	\$ 132,861,006
Mortgage repayments on refinancing	(38,066,147)
Interim financing	<u>24,900,000</u>
	119,694,859
Principal repayments	(6,771,886)
Change in the difference between contractual and market interest rates on mortgage loans assumed	(190,262)
Change in the unamortized component of transaction costs	<u>(139,593)</u>
	<u>\$ 112,593,118</u>

A summary of interest rates and debt ratios for the mortgage loan portfolio is provided in the following chart.

Mortgage Loan Debt Summary

	2008			
	December 31	September 30	June 30	March 31
Weighted average interest rate				
Fixed rate mortgage loans	6.4%	6.4%	6.4%	6.2%
Floating rate mortgage loans	5.9%	5.9%	5.9%	6.4%
Ratio of mortgage loans payable, compared to: *				
Purchase price of income-producing properties	76%	77%	78%	81%
Appraised value of property portfolio	63%	64%	63%	68%
Ratio of mortgage loans payable and convertible debenture debt (at face value), compared to acquisition cost of income-producing properties	85%	86%	96%	90%

	2007			
	December 31	September 30	June 30	March 31
Weighted average interest rate				
Fixed rate mortgage loans	6.0%	6.3%	6.2%	6.3%
Floating rate mortgage loans	7.1%	7.4%	7.1%	7.4%
Ratio of mortgage loans payable, compared to: *				
Purchase price of income-producing properties	80%	82%	82%	78%
Appraised value of property portfolio	67%	66%	66%	79%
Ratio of mortgage loans payable and convertible debenture debt (at face value), compared to acquisition cost of income-producing properties	89%	96%	99%	93%

* Ratio is calculated for all properties with mortgage loans payable and excludes properties with acquisition cost payable.

Interim Mortgage Loan Financing

As of December 31, 2008, the mortgage loans payable of LREIT includes \$53.4 Million of interim mortgage loan financing, comprised of the following:

<u>Amount</u>	<u>Maturity Date</u>
\$4.5 Million	January 1, 2009
\$5.4 Million	January 1, 2009
\$4.0 Million	April 1, 2009
\$2.0 Million	September 1, 2009
\$7.5 Million	November 1, 2009
\$12.0 Million	October 30, 2010
\$18.0 Million	October 31, 2010
<u>\$53.4 Million</u>	

The interim mortgage loans are secured by charges registered against two or more income properties, aside from the \$2 Million loan which is registered against one income property. The loans bear interest at a weighted average rate of 9.6% and require payments of interest only.

The \$4.5 Million interim mortgage loan which matured on January 1, 2009 was renewed for a six month term in order to coincide with the maturity date of a related loan. The \$5.4 Million interim mortgage loan which matured on January 1, 2009 and the \$4 Million loan which matures on April 1, 2009 were renewed for one year terms.

Vendor Take-Back Mortgages

Mortgage loans payable include \$5.6 Million of interest-only vendor take-back mortgage loans, as follows:

- a \$1,600,000 vendor take-back mortgage, bearing interest at a rate of 6.25%, obtained upon the purchase of Westhaven Manor in May 2007. The loan is repayable on demand.
- a \$4,000,000 vendor take-back mortgage, bearing interest at a rate of 5%, obtained upon the acquisition of Siena Apartments in July 2008. The loan matures on July 1, 2010.

Revolving Line of Credit

The Trust utilizes a revolving line of credit with an authorized limit of \$5 Million. The line of credit bears interest at the Royal Bank prime rate. As of December 31, 2008, the amount available on the line of credit was \$1.55 Million.

Financing of Acquisition Costs Payable**Millennium Village**

Millennium Village was acquired in four phases during 2007 with the final closing date for the entire property occurring in November 2007. In accordance with the terms of the purchase agreement, the balance owing on the purchase price of Millennium Village was paid in May 2008.

The payment was funded by a new floating interest rate mortgage of \$22,781,500. The interest rate of the mortgage was fixed at 5.82% with the use of an interest rate swap arrangement.

Parsons Landing

As previously disclosed in this report, the purchase agreement for Parsons Landing provided for a portion of the \$63.2 Million purchase price to be paid subsequent to the possession date of the property. The balance payable on Parsons Landing was approximately \$48.2 Million as of December 31, 2008.

As a result of a delay in the funding of the mortgage loan financing for the property, the payment of the balance owing has been delayed. The date of payment of the balance owing has been extended to May 29, 2009, with interest. It is anticipated that the first mortgage loan financing for Parsons Landing will be completed in the second quarter of 2009.

Interest Charges on Unpaid Purchase Price

As noted above, a portion of the purchase price of Millennium Village and Parsons Landing was paid subsequent to the possession date of the properties and possession of both properties was acquired in phases. Interest on the balance owing is capitalized until the property achieves the level of occupancy required to be classified as an income property. Subsequent to the classification as an income property, interest on the balance owing is charged to mortgage loan interest expense.

SELECTED ANNUAL INFORMATION

	2008	2007	2006 (restated)
Distributions			
Total	\$ 10,029,556	\$ 9,967,360	\$ 9,766,357
Per unit	\$ 0.56	\$ 0.56	\$ 0.56
Balance Sheet			
Total assets	\$ 602,188,330	\$ 476,199,270	\$ 294,222,201
Total face value of mortgage loans payable and convertible debentures	\$ 507,554,133	\$ 396,224,160	\$ 226,106,511
Operating Results			
Total revenue	\$ 66,802,294	\$ 46,311,315	\$ 30,538,848
Loss for the year	\$ (9,607,056)	\$ (1,400,904)	\$ (3,152,367)
Per unit Loss for the year			
Per unit - basic	\$ (0.549)	\$ (0.080)	\$ (0.184)
Per unit - diluted	\$ (0.549)	\$ (0.080)	\$ (0.184)

ANALYSIS OF INCOME/LOSS**Changes in Property Portfolio**

The ongoing growth in the portfolio of income-producing properties of LREIT is one of the main factors affecting the comparability of financial results in different reporting periods. During the period between January 1, 2007 and December 31, 2008, the portfolio of income-producing properties increased by approximately \$318 Million, based on property purchase prices, of which approximately \$268 Million or 84% pertains to new income-producing properties located in Fort McMurray, Alberta, including Parsons Landing. The increase in the Fort McMurray portfolio occurred relatively evenly throughout 2007 and 2008.

After pro-rating property purchase prices, based on the month of acquisition or possession, the cost base of the portfolio of income-producing properties of LREIT was approximately \$147 Million greater in 2008, in comparison to the cost base for the portfolio in 2007.

Properties which were added to the income-producing portfolio during 2007 and 2008 are as follows:

2007

- Nova Court, Yellowknife - March 2007
- Woodland Park, Fort McMurray - April 2007
- Sir Robert Borden Place, Saskatoon - May 2007
- Westhaven Manor, Edson - May 2007
- Lakewood Manor, Fort McMurray - July 2007
- Millennium Village, Fort McMurray - November 2007

2008

- Laird's Landing, Fort McMurray - June 1, 2008
- Siena Apartments, Fort McMurray - July 2, 2008
- Parsons Landing, Fort McMurray - September 1, 2008 (i)
- Colony Square, Winnipeg - October 1, 2008

(i) LREIT took possession of Parsons Landing on September 1, 2008. See "Property Acquisitions - Parsons Landing" above.

Overall Results

A comparison of the 2008 and 2007 financial results of LREIT is provided in the following chart. As disclosed on the chart, income before amortization, non-controlling interest and taxes increased by \$1,155,073 during 2008, compared to 2007. The increase mainly reflects an increase in net operating income, partially offset by an increase in financing expense and trust expense.

The increase in net operating income mainly reflects an increase in rental revenue, partially offset by an increase in property operating costs.

After including amortization charges, non-controlling interest and future income taxes, LREIT incurred a loss of \$9,607,056 during 2008, compared to a loss of \$1,400,904 in 2007.

A detailed analysis of the above noted variables is provided in the following sections of this report.

Analysis of Loss

	Year ended December 31		Increase (decrease)	
	2008	2007	Amount	%
Rental revenue	\$ 65,847,271	\$ 45,216,274	\$ 20,630,997	45.6 %
Interest and other income	955,023	1,095,041	(140,018)	(12.8)%
Property operating costs	<u>24,732,149</u>	<u>19,238,660</u>	<u>5,493,489</u>	<u>28.6 %</u>
Net operating income (NOI) *	42,070,145	27,072,655	14,997,490	55.4 %
Trust expense	<u>2,622,973</u>	<u>2,056,789</u>	<u>566,184</u>	<u>27.5 %</u>
Income before financing expense, amortization, non-controlling interest and taxes (EBITDA) *	39,447,172	25,015,866	14,431,306	57.7 %
Financing expense	<u>36,291,778</u>	<u>23,015,545</u>	<u>13,276,233</u>	<u>57.7 %</u>
Income before amortization, non-controlling interest and taxes *	3,155,394	2,000,321	1,155,073	57.7 %
Amortization	11,408,548	8,174,795	3,233,753	39.6 %
Non-controlling interest	<u>(87,860)</u>	<u>40,707</u>	<u>(128,567)</u>	<u>(315.8)%</u>
Loss before future income tax *	(8,341,014)	(6,133,767)	(2,207,247)	36.0 %
Future income tax expense (recovery)	<u>1,266,042</u>	<u>(4,732,863)</u>	<u>5,998,905</u>	<u>(126.8)%</u>
Loss for the year	<u>\$ (9,607,056)</u>	<u>\$ (1,400,904)</u>	<u>\$ (8,206,152)</u>	<u>585.8 %</u>

* The analysis of loss for the year represents the re-formatting of balances from the Consolidated Statements of Operations in order to provide a summarized analysis of the financial performance of the Trust. All of the lines in the analysis agree to amounts in the financial statements. Accordingly, the analysis consists entirely of GAAP measurements, aside from the four sub-totals (see asterisks).

Revenue

Total Revenue

Analysis of Total Revenue

	Income Properties		Trust
	Residential	Commercial	
Rental revenue	93%	7%	n/a
Interest and other income	49%	4%	47%
Total revenue	93%	6%	1%

Increase in Total Revenue

	Total Revenues			
	Year ended December 31		Increase (decrease)	
	2008	2007	Amount	% of Total
Residential	\$ 61,850,340	\$ 41,032,962	\$ 20,817,378	102 %
Commercial	4,502,185	4,544,175	(41,990)	(1)%
Trust	449,769	734,178	(284,409)	(1)%
Total	<u>\$ 66,802,294</u>	<u>\$ 46,311,315</u>	<u>\$ 20,490,979</u>	<u>100 %</u>

Residential Properties

As disclosed in the first chart above, the revenue of LREIT is primarily generated from the portfolio of residential properties. During 2008, the portfolio of residential properties accounted for 93% of total revenues of the Trust.

As disclosed in the second chart above, the growth in the revenue of LREIT is entirely attributable to the portfolio of residential properties. During 2008, the total revenue of LREIT increased by approximately \$20.5 Million, compared to 2007, comprised of an increase of \$20.8 Million in the revenue of residential property portfolio, partially offset by a decrease in revenue from the commercial property portfolio and from general Trust operations.

Commercial Properties

Total Revenues

During 2008, the portfolio of four commercial properties accounted for 6% of total revenue of LREIT. In comparison to 2007, the revenue of the commercial portfolio decreased by \$41,990 during 2008, primarily due to the loss of revenue from the MAAX Warehouse, effective July 1, 2008, as well as an increase in vacancy loss at the Kenaston Property.

Warehouse Building at 156 and 204 East Lake Boulevard, Airdrie, Alberta

The commercial properties in the real estate portfolio of LREIT include a 39,936 square foot warehouse building in Airdrie, Alberta. Since the acquisition of the property in June 2003, the warehouse building was 100% leased to MAAX Inc. Effective July 1, 2008, MAAX Inc. successfully filed for creditor protection and discontinued rent payments. Pending the releasing of the property, the reduction in revenue from the loss of the MAAX Warehouse lease will have a minimal impact on the overall financial position and results of operation of the Trust.

Trust Operations

Revenue from Trust operations is comprised almost exclusively of interest income on mortgage loans receivable and cash. The revenue is classified as "interest and other income" and represents a minor component of the overall revenues of the Trust.

As disclosed on the first chart above, revenue from Trust operations accounted for 1% of the total revenue of LREIT during 2008. In comparison to 2007, revenue from Trust operations decreased by \$284,409 during 2008, mainly due to a reduction in interest income on mortgage loans receivable.

Rental Revenue from Residential Properties

Overall Increase

As noted above, revenue from residential properties increased by \$20,817,378 during 2008. The increase is comprised of a \$20,679,815 increase in rental revenue and a \$137,563 increase in interest and other income.

The increase in residential rental revenue is mainly attributable to the acquisition of additional residential properties, as well as an improvement in the operating results of the residential properties which have been in the LREIT portfolio since January 1, 2007.

Analysis of Revenue from Residential Properties by Geographic Segment

Analysis of Revenue from Residential Properties

	Year Ended December 31					
			Increase (decrease)		Percentage of Total	
	2008	2007	Amount	%	2008	2007
Alberta						
Fort McMurray	\$ 33,861,758	\$ 16,787,712	\$ 17,074,046	102 %	55 %	41 %
Other Alberta	4,393,078	3,830,708	562,370	15 %	7 %	9 %
Total - Alberta	38,254,836	20,618,420	17,636,416	86 %	62 %	50 %
Saskatchewan	11,755,250	10,567,988	1,187,262	11 %	19 %	26 %
Northwest Territories	6,039,137	5,080,095	959,042	19 %	10 %	12 %
Manitoba	2,880,752	1,662,240	1,218,512	73 %	5 %	4 %
British Columbia	1,479,656	1,453,273	26,383	2 %	2 %	4 %
Ontario	1,440,709	1,650,946	(210,237)	(13)%	2 %	4 %
Total Residential Portfolio	<u>\$ 61,850,340</u>	<u>\$ 41,032,962</u>	<u>\$ 20,817,378</u>	<u>51 %</u>	<u>100 %</u>	<u>100 %</u>

Analysis of Vacancy Loss for Residential Properties

	Vacancy Loss	
	2008	2007
Alberta		
Fort McMurray	4 %	4 %
Other Alberta	2 %	2 %
Total - Alberta	4 %	4 %
Saskatchewan	3 %	6 %
Northwest Territories	0 %	0 %
Manitoba	4 %	15 %
British Columbia	5 %	3 %
Ontario	34 %	14 %
Total Residential Portfolio	4 %	5 %

The acquisition of additional properties in Fort McMurray during 2008 resulted in a significant increase in the percentage of revenues contributed by the Fort McMurray property portfolio. As disclosed on the first chart above, revenues from residential properties in Fort McMurray increased by \$17,074,046, compared to 2007, representing 82% of the total increase in residential rental revenue. As a percentage of total rental revenues, the contribution by the Fort McMurray portfolio increased from 41% during 2007 to 55% during 2008.

The property portfolios in Saskatchewan and the Northwest Territories maintained a ranking of second and third position in terms of overall revenue contributions, as a result of relative size of the portfolios and the acquisition of an additional property in each location in 2007.

The decrease in revenue for the Ontario portfolio is mainly due to the temporary increase in vacancy associated with the expansion of Elgin Lodge.

Operating Costs

Analysis of Operating Costs

	Property Operating Costs		Increase (decrease)	
	2008	2007	Amount	%
Alberta				
Fort McMurray	\$ 8,766,334	\$ 4,550,029	\$ 4,216,305	93 %
Other Alberta	1,787,550	1,773,381	14,169	1 %
Total - Alberta	10,553,884	6,323,410	4,230,474	67 %
Saskatchewan	6,417,800	6,093,955	323,845	5 %
NWT	2,459,794	2,057,851	401,943	20 %
Manitoba	1,206,966	873,556	333,410	38 %
British Columbia	875,505	872,868	2,637	- %
Ontario	987,350	1,169,673	(182,323)	(16)%
Total Residential Portfolio	22,501,299	17,391,313	5,109,986	29 %
Total Commercial Portfolio	2,230,850	1,847,347	383,503	21 %
Total	\$ 24,732,149	\$ 19,238,660	\$ 5,493,489	29 %

During 2008, property operating costs for the residential portfolio increased by \$5,109,986 or 29%, compared to 2007, with the Fort McMurray portfolio accounting for the majority of the increase due to the additional property acquisitions in Fort McMurray, subsequent to January 1, 2007. The property portfolio in the Northwest Territories and in Saskatchewan account for the majority of the remaining increase in property operating costs. For the Northwest Territories portfolio, the increase in property operating costs is mainly due to the acquisition of Nova Court on March 22, 2007. Similarly, for the Saskatchewan portfolio, the increase in property operating costs is mainly due to the acquisition of Sir Robert Borden Place on May 1, 2007.

As with the revenue decrease, the decrease in operating costs for the Ontario portfolio in 2008, is also mainly due to the temporary increase in vacancy associated with the expansion of Elgin Lodge.

Net Operating Income and Operating Margin

Overall

Summary Analysis of Net Operating Income

	Net Operating Income			Operating Margin	
	Amount		Increase (decrease)	2008	2007
	2008	2007			
Residential	\$ 39,349,041	\$ 23,641,647	\$ 15,707,394	64 %	58 %
Commercial	2,271,335	2,696,830	(425,495)	50 %	59 %
Trust	449,769	734,178	(284,409)	n/a	n/a
Total	<u>\$ 42,070,145</u>	<u>\$ 27,072,655</u>	<u>\$ 14,997,490</u>	63 %	58 %

After reflecting "interest and other income" from Trust operations, the net operating income ("NOI") of the Trust increased by \$14,997,490 during 2008, compared to 2007. The increase in total NOI reflects a significant increase in NOI from the residential portfolio and a modest decrease in NOI from the commercial portfolio and from general "Trust" operations.

Residential Properties

During 2008, the NOI for the residential portfolio increased by \$15,707,394 or 66%, compared to 2007. The increase in NOI for the residential property portfolio mainly reflects the new income-producing properties in Fort McMurray and the fact that the operating margin for the Fort McMurray portfolio continues to be significantly higher in comparison to properties in other locations. Please refer to the following chart.

Analysis of Net Operating Income - Residential Properties

	Net Operating Income							
	Year ended December 31		Increase (decrease)		Percent of Total		Operating Margin	
	2008	2007	Amount	%	2008	2007	2008	2007
Alberta								
Fort McMurray	\$ 25,095,423	\$ 12,237,679	\$ 12,857,744	105 %	64 %	52 %	74 %	73 %
Other Alberta	2,605,528	2,057,327	548,201	27 %	7 %	9 %	59 %	54 %
Total - Alberta	27,700,951	14,295,006	13,405,945	94 %	71 %	61 %	72 %	69 %
Saskatchewan	5,337,450	4,474,035	863,415	19 %	14 %	19 %	45 %	42 %
Northwest Territories	3,579,343	3,022,244	557,099	18 %	9 %	13 %	59 %	59 %
Manitoba	1,673,785	788,683	885,102	112 %	4 %	3 %	58 %	47 %
British Columbia	604,151	580,405	23,746	4 %	2 %	2 %	41 %	40 %
Ontario	453,359	481,274	(27,915)	(6)%	1 %	2 %	31 %	29 %
Total Residential Portfolio	<u>\$ 39,349,039</u>	<u>\$ 23,641,647</u>	<u>\$ 15,707,392</u>	<u>66 %</u>	<u>100 %</u>	<u>100 %</u>	<u>64 %</u>	<u>58 %</u>

During 2008, the NOI from the Fort McMurray portfolio increased by \$12.9 Million, representing 82% of the total increase in the NOI from the residential property portfolio. The operating margin for the Fort McMurray portfolio remained high at 74% during 2008, compared to an average of 51% for the remainder of the residential property portfolio.

The most significant change in the operating margin occurred in the Manitoba portfolio, with the margin increasing from 47% in 2007 to 58% in 2008. The improvement in the Manitoba portfolio mainly reflects the completion of the major renovation program at Highland Tower, as well as the positive results for Colony Square for the fourth quarter of 2008.

Overall, the operating margin for the property portfolio increased to 64% in 2008, compared to 58% in 2007.

Same Property Analysis - Residential Properties

The same property analysis for 2008 encompasses the 28 income-producing residential properties which were in the LREIT portfolio, as of January 1, 2007. (Highland Tower is excluded from the same property analysis as a major in-suite renovation program was in process during the first six months of 2007 and a significant number of suites were not available to the rental market.)

As disclosed in the following analysis, the revenue of the same properties increased by 8.6%, while net operating income increased by 10.7%. The improvement in net operating income is mainly attributable to the improvement in the operating margins arising from increases in rental rates partially offset by increased property operating costs. Specifically, the improvement in same property NOI reflects rental rate increases and an improvement in occupancy levels at the majority of the "same" properties.

	Year Ended December 31		Increase	
	2008	2007	Amount	%
Total revenue	\$ 34,049,339	\$ 31,342,576	\$ 2,706,763	8.6 %
Net operating income	\$ 18,990,345	\$ 17,148,857	\$ 1,841,488	10.7 %

Trust Expense

Trust expense increased by \$566,184 during 2008, compared to 2007. The increase mainly reflects an increase of \$484,341 in the service fee of Shelter Canadian in regard to administrative and asset management services due to the increased size of the Trust's assets. The fee is equal to 0.3% of the net book value of the assets of LREIT, excluding cash and accumulated amortization, as of the date of the most recently issued financial statements.

Please refer to "Related Party Transactions" for additional information in regard to the administrative, asset management and property management services which are provided to LREIT by Shelter Canadian Properties Limited and the associated remuneration.

Financing Expense

Financing expense increased by \$13,276,233 or 58% during 2008, compared to 2007, comprised of a \$12,984,804 increase in mortgage loan financing expense and \$291,429 increase in convertible debenture financing expense.

Financing expense encompasses mortgage loan and convertible debenture interest, as well as a number of "non-cash" expenses, including amortization charges for transaction costs, accretion and the change in fair value of interest rate swap. During 2008, "non-cash" expenses represented 22.7% of the total financing expenses, compared to 16.4% in 2007.

Analysis of Financing Expense

	Year ended December 31		Increase (decrease)	
	2008	2007	Amount	%
Mortgage Loans				
Mortgage loan interest	\$ 24,116,087	\$ 15,092,084	\$ 9,024,003	60 %
Amortization of transaction costs	1,159,912	1,211,514	(51,602)	(4)%
Change in value - swap assets	4,012,403	-	4,012,403	-
Total - mortgage loans	29,288,402	16,303,598	12,984,804	80 %
Debentures				
Interest on convertible debentures	3,943,760	4,159,555	(215,795)	(5)%
Accretion of debt component	2,469,702	2,004,220	465,482	23 %
Amortization of transaction costs	589,914	548,172	41,742	8 %
Total - debentures	7,003,376	6,711,947	291,429	4 %
Total - financing expense	\$ 36,291,778	\$ 23,015,545	\$ 13,276,233	58 %

Interest Expense - Mortgage Loans

Mortgage loan interest increased by \$9,024,003 or 60% during 2008, compared to 2007. The increase reflects the increase in mortgage loan debt, as discussed in the "Mortgage Loans Payable" section of this report and interest on the balance owing in regard to the acquisition of Parsons Landing.

Interest Expense - Debentures

During 2008, interest on convertible debentures decreased by \$215,795 or 5%, compared to 2007. The decrease mainly reflects the retirement of \$1.6 Million of Series D Convertible Debentures in March 2008.

Total Interest Expense

As a percentage of operating income, total interest for mortgage loans and convertible debentures decreased from 71% during 2007, to 67% during 2008. The decrease in the ratio of interest, relative to operating income, reflects the extent to which the increase in net operating income has exceeded the increase in interest expense during 2008, due to the following inter-related factors:

- (i) an improvement in NOI returns from the asset base of the Trust, particularly in regard to properties which progressed from the development stage to the income-producing stage;
- (ii) a decrease in the amount of convertible debenture debt; partially offset by
- (iii) an increase in the weighted average interest rate of fixed rate mortgage loans.

Change in Value of Swap Asset

As disclosed in the preceding chart, the increase in financing expense in 2008 includes an amount of \$4,012,403 related to the change in value of an "interest rate swap".

During 2008, LREIT entered into interest rate swap arrangements whereby the interest rate on two floating rate mortgages were fixed for the five and ten year terms of the mortgages. The main purpose of the interest rate swap arrangement is to reduce the risk associated with floating interest rates. The interest rate swap agreement is a derivative financial instrument and it is recorded at "fair value" on the balance sheet of the Trust. Changes in fair value are recognized as earnings/losses through charges to financing expense. Increases in fair value serve to decrease financing expense, while decreases in fair value serve to increase financing expense.

In very general terms, the fair value of the interest rate swap is based on the difference between the net present value of projected payments under the fixed rate mortgage, compared to the net present value of projected payments under the floating rate mortgage. During 2008, the fair value of the interest rate swap arrangement decreased by \$4,012,403, as declining market interest rates in the fourth quarter of 2008 served to reduce payments for mortgages with floating interest rates.

Although the decrease in the fair value of the interest rate swap has resulted in a corresponding increase in the loss of LREIT, the "decrease in value" is a non-cash expense which is added back for purposes of determining the operating cash flow of the Trust. As a result of fluctuations in market interest rates, the value of the interest rate swap may fluctuate significantly from quarter to quarter, however, the change in value has no impact on cash outflows throughout the entire term of the swap agreement. The change in value provides an indication of the relative benefit of a fixed rate mortgage, compared to a floating rate mortgage, during a specified period of time.

The quarterly fluctuation is particularly evident in the fourth quarter results for LREIT, as the fair value of the interest rate swap changed from a positive amount of \$1,204,002, as of September 30, 2008, to a negative amount of \$4,012,403 as of December 31, 2008, representing a reduction in value of \$5,216,405. The decrease in value served to increase financing expense by \$5,216,405 in the fourth quarter of 2008 and effectively skewed the comparative analysis of the third and fourth quarter results of the Trust.

Amortization Expense

During 2008, amortization expense increased by \$3,233,753 or 40%, compared to 2007. The increase is mainly due to amortization charges for the income-producing properties which have been added to the LREIT property portfolio during 2007 and 2008. Amortization expense on the Consolidated Statement of Loss excludes amortization charges for transaction costs.

Future Income Taxes

LREIT currently qualifies for special income tax treatment whereby distributions are deductible for purposes of calculating the taxable income of the Trust. The deductibility of distributions serves to reduce the taxable income of the Trust to nil and eliminate the need to claim capital cost allowance.

In 2011, LREIT may no longer qualify for special tax treatment and, as such, distributions would no longer be deductible for income tax purposes. In accordance with generally accepted accounting principles, LREIT is calculating a future income tax asset in the event that LREIT loses its special tax treatment in 2011. The future income tax asset is based on the temporary difference between the accounting and tax basis of assets held by the Trust.

In addition, the wholly-owned subsidiaries, which hold the operations of the seniors housing complexes, are operating businesses and account for future income tax assets and liabilities by recognizing the temporary differences between tax and accounting bases of assets and liabilities, as well as the benefit of operating losses available to be carried forward to future years for income tax purposes, net of an allowance to recognize the uncertainty of the benefit of the operating losses (the "valuation allowance"). Current income taxes are recorded when payable. In 2008, the valuation allowance served to reduce the tax asset relating to operating losses to nil.

The estimate of the future income tax assets and liabilities, is subject to periodic change. To the extent that the net future income tax position increases or decreases, there is a corresponding increase or decrease in the future income tax expense or recovery of the Trust, with the increase or decrease having a direct impact on bottom-line results.

As of December 31, 2008, future income tax liabilities exceeded future income tax assets resulting in a net liability position of \$88,766, compared to a net asset position of \$1,145,856 as of December 31, 2007. The change in the estimated net future income tax position on the balance sheet resulted in a future income tax expense of \$1,234,622. The income tax expense is increased by current income tax payable by a wholly-owned subsidiary of \$31,420.

The future income tax expense of \$1,234,622 is a non-cash item which does not affect the cash flow of the Trust. The cumulative amount of future income tax expenses/recoveries relating to the assets of the Trust are subject to reversal in the event that LREIT maintains its current tax status in 2011.

Comparison to Preceding Quarter

Analysis of Loss - Fourth Quarter 2008 vs. Third Quarter 2008

	Three months ended		Increase (decrease)	
	December 31, 2008	September 30, 2008	Amount	%
Rental revenue	\$ 19,984,545	\$ 17,817,076	\$ 2,167,469	12.2 %
Interest and other income	290,875	105,547	185,328	175.6 %
Property operating costs	<u>7,063,497</u>	<u>6,126,342</u>	<u>937,155</u>	<u>15.3 %</u>
Net Operating Income (NOI)	13,211,923	11,796,281	1,415,642	12.0 %
Trust expense	<u>755,661</u>	<u>580,409</u>	<u>175,252</u>	<u>30.2 %</u>
Income before financing expense, amortization, non-controlling interest and taxes (EBITDA)	12,456,262	11,215,872	1,240,390	11.1 %
Financing expense	<u>14,861,476</u>	<u>7,711,151</u>	<u>7,150,325</u>	<u>92.7 %</u>
Income (loss) before amortization, non-controlling interest and taxes	(2,405,214)	3,504,721	(5,909,935)	(168.6)%
Amortization	3,600,150	3,085,470	514,680	16.7 %
Non-controlling interest	<u>30,362</u>	<u>18,993</u>	<u>11,369</u>	<u>59.9 %</u>
Income (loss) before future income tax expense (recovery)	(6,035,726)	400,258	(6,435,984)	(1,608.0)%
Future income tax expense (recovery)	<u>(3,850,378)</u>	<u>2,833,456</u>	<u>(6,683,834)</u>	<u>(235.9)%</u>
Loss for the period	<u>\$ (2,185,348)</u>	<u>\$ (2,433,198)</u>	<u>\$ 247,850</u>	<u>(10.2)%</u>

During the fourth quarter of 2008, LREIT incurred a loss of \$2,405,214 before amortization, non-controlling interest and future income tax recovery compared to income of \$3,504,721 during the third quarter of 2008.

As previously discussed in the analysis of financing expense for 2008, the fourth quarter results reflect a decrease in the fair value of the interest rate swap of \$5,216,405. The decrease in the fair value served to increase financing expense in the fourth quarter by \$5,216,405. In the absence of the entries to record the change in fair value of the interest rate swap, LREIT generated income, before amortization, non-controlling interest and taxes of \$2,811,191 in the fourth quarter of 2008, compared to income of \$2,300,719 in the third quarter of 2008, representing an increase of approximately \$500,000.

The increase mainly reflects an increase in net operating income of approximately \$1.4 Million, partially offset by a \$800,000 increase in financing expense, net of the amount pertaining to the interest rate swap.

The increase in operating income and financing expense, as adjusted, mainly reflects the incremental income and financing expenses related to the acquisition of Colony Square on October 1, 2008 and the operations of Phase II of Parsons Landing for an entire quarter.

After providing for amortization charges, non-controlling interest and future income tax expense/recoveries, LREIT completed the three month period ended December 31, 2008 with a loss of \$2,185,348, compared to a loss of \$2,433,198 during the third quarter of 2008. The bottom-line results reflect an \$6.7 Million decrease in the future income tax expense which more than offsets the \$5.2 Million increase in financing expense pertaining to the interest rate swap. The significant change in the provision for future income taxes mainly reflects an adjustment to the future estimated taxable income of the Trust.

The change in the value of the interest rate swap and the change in the future income tax recovery/expense are non-cash transactions, as are the fourth quarter amortization charges and the component of the fourth quarter financing expenses pertaining to the accretion of the convertible debentures. The extent of non-cash transactions is reflected in the fourth quarter cash flow results, as evidenced by the fact that the cash from operating activities increased by approximately \$5.7 Million during the fourth quarter of 2008, compared to the third quarter of 2008.

Summary of Quarterly Results

Quarterly Analysis

	2008			
	Q4	Q3	Q2	Q1
Total revenue	\$ 19,984,545	\$ 17,922,623	\$ 14,975,258	\$ 13,628,993
Net operating income	\$ 13,211,923	\$ 11,796,281	\$ 9,111,999	\$ 7,949,942
Income (loss) for the period	\$ (2,185,348)	\$ (2,433,198)	\$ (4,988,811)	\$ 301
Gain (loss) for the period, before future income tax	\$ (6,035,726)	\$ 400,258	\$ (752,648)	\$ (1,952,898)

PER UNIT

Net operating income				
- basic	\$ 0.758	\$ 0.673	\$ 0.520	\$ 0.455
- diluted	\$ 0.519	\$ 0.463	\$ 0.357	\$ 0.312
Income (loss) for the period				
- basic	\$ (0.125)	\$ (0.139)	\$ (0.284)	\$ -
- diluted	\$ (0.125)	\$ (0.139)	\$ (0.284)	\$ -
Loss for the period, before future income tax				
- basic	\$ (0.346)	\$ 0.023	\$ (0.043)	\$ (0.112)
- diluted	\$ (0.346)	\$ 0.023	\$ (0.043)	\$ (0.112)

Quarterly Analysis

	2007			
	Q4	Q3	Q2	Q1
Total revenue	\$ 13,534,875	\$ 12,597,091	\$ 11,127,584	\$ 9,051,765
Net operating income	\$ 7,822,808	\$ 7,845,308	\$ 6,519,763	\$ 4,884,730
Income (loss) for the period	\$ (1,108,898)	\$ 725,735	\$ 688,355	\$ (1,706,093)
Loss for the period, before future income tax	\$ (1,742,327)	\$ (1,188,347)	\$ (1,417,123)	\$ (1,032,626)

PER UNIT

Net operating income				
- basic	\$ 0.447	\$ 0.449	\$ 0.374	\$ 0.281
- diluted	\$ 0.330	\$ 0.331	\$ 0.295	\$ 0.255
Income (loss) for the period				
- basic	\$ (0.064)	\$ 0.042	\$ 0.039	\$ (0.033)
- diluted	\$ (0.064)	\$ 0.042	\$ 0.039	\$ (0.033)
Loss for the period, before future income tax				
- basic	\$ (0.100)	\$ (0.068)	\$ (0.081)	\$ (0.060)
- diluted	\$ (0.100)	\$ (0.068)	\$ (0.081)	\$ (0.060)

Loss Per Unit

Analysis of Loss per Unit

	Year ended December 30		Change	
	2008	2007		
Income (loss) for the year				
- basic	\$ (0.549)	\$ (0.080)	\$ (0.469)	(586)%
- diluted	\$ (0.549)	\$ (0.080)	\$ (0.469)	(586)%
Loss for the period, before future income tax				
- basic	\$ (0.477)	\$ (0.351)	\$ (0.126)	(36)%
- diluted	\$ (0.477)	\$ (0.351)	\$ (0.126)	(36)%

Excluding future income tax, LREIT incurred a loss of \$0.477 per unit during 2008, compared to a loss of \$0.351 per unit during 2007. As the weighted average number of units only increased by 0.3% during 2008, the increase in the loss per unit mainly reflects the increase in the overall loss of the Trust before future income tax.

The increase in the loss before future tax expense (recovery) is primarily due to the extent of non-cash expenses. In comparison, cash from operating activities increased from \$0.406 per unit in 2007 to \$0.710 per unit in 2008. An analysis of the improvement in cash from operating activities is provided below.

ANALYSIS OF CASH FLOWS

Operating Activities

Cash from Operating Activities

	Year ended December 31		Increase (decrease)
	2008	2007	
Rental revenue	\$ 65,847,271	\$ 45,216,274	\$ 20,630,997
Interest and other income	955,023	1,095,041	(140,018)
Property operating costs	24,732,149	19,238,660	5,493,489
Net operating income (NOI)	42,070,145	27,072,655	14,997,490
Non-cash components of revenue	9,129	57,019	(47,890)
	42,061,016	27,015,636	15,045,380
Financing expense	36,291,778	23,015,545	13,276,233
Non-cash component of financing expense	8,231,931	3,763,906	4,468,025
	28,059,847	19,251,639	8,808,208
Trust expense	2,622,973	2,056,789	566,184
Non-cash component of trust expense	391,517	309,233	82,284
	2,231,456	1,747,556	483,900
Cash provided by operating activities, before changes in non-cash operating activities, tenant inducements and leasing expenses	11,769,713	6,016,441	5,753,272
Tenant inducements and leasing expenses	592,552	105,479	487,073
	11,177,161	5,910,962	5,266,199
Changes in non-cash operating items	1,238,353	1,168,265	70,088
Cash provided by operating activities	\$ 12,415,514	\$ 7,079,227	\$ 5,336,287

During 2008, LREIT generated cash from operating activities of \$12,415,514. After excluding changes in non-cash operating items, cash from operating activities increased by \$5,266,199 or 89% during 2008, compared to 2007. The increase mainly reflects an increase in net operating income, partially offset by an increase in the cash component of financing expense and, to a lesser extent, by an increase in Trust expense and an increase in tenant inducements and leasing expense. Specifically, net operating income increased by \$14,997,490, while the cash component of financing expense increased by \$8,808,208, the cash component of Trust expense increased by \$483,900, and tenant inducements and leasing expenses increased by \$487,073.

As disclosed in the preceding analysis of financing expense, the cash component of financing expense reflects mortgage loan interest and convertible debenture interest and is calculated by excluding amortization of transaction costs, the change in the fair value of the swap asset and the accretive portion of the debt component of convertible debentures. As previously discussed, the increase in mortgage loan interest accounts for the majority of the increase in the cash component of financing expense. The increase in mortgage loan interest is mainly attributable to the mortgage financing for new property acquisitions, as well as accrued interest on the balance owing in regard to the acquisition of Parsons Landing.

The cash component of trust expense increased by \$483,900 during 2008, mainly due to an increase in the service fee of Shelter Canadian. The cash component of trust expense excludes unit compensation expense.

During 2008, the cash outflow in regard to tenant inducements and leasing expenses amounted to \$592,552. The tenant inducements and leasing expenses are mainly in regard to new tenancies at the Kenaston property.

Overall, the increase in cash from operating activities for 2008 reflects an ongoing improvement in the NOI return on the total asset base of the Trust, net of the cash component of financing expense.

Funds from Operations ("FFO") & Adjusted Funds from Operations ("AFFO")

LREIT considers "Funds from Operations" ("FFO") and "Adjusted Funds from Operations" ("AFFO") to be meaningful additional measures of operating performance. FFO measures the cash generating abilities of LREIT, while AFFO is indicative of available cash flow after capital reinvestment transactions.

During 2008, FFO increased by \$1,155,073, compared to 2007, while AFFO increased by \$5,156,349. On a basic per unit basis, FFO increased by \$0.065 per unit, while AFFO increased by \$0.295 per unit.

Funds from Operations/Adjusted Funds from Operations *

	Year Ended December 31	
	2008	2007
Income (loss) for the year	\$ (9,607,056)	\$ (1,400,904)
Add (deduct):		
Amortization expense	11,408,548	8,174,795
Future income tax	1,266,042	(4,732,863)
Non-controlling interest	87,860	(40,707)
Funds from operations *	3,155,394	2,000,321
Add (deduct):		
Straight-line rent adjustment	(10,903)	(58,618)
Net amortization of above/below market in-place leases	1,774	1,599
Accretion of debt component of convertible debentures	2,469,702	2,004,220
Unit-based compensation	391,517	309,233
Change in fair value of interest rate swap	4,012,403	-
Tenant inducement and leasing expenses	(592,552)	(105,479)
Ongoing improvements to income properties	(1,374,279)	(1,254,569)
Adjusted funds from operations *	\$ 8,053,056	\$ 2,896,707
FFO per unit *		
- basic	\$ 0.180	\$ 0.115
- diluted	\$ 0.172	\$ 0.112
AFFO per unit *		
- basic	\$ 0.461	\$ 0.166
- diluted	\$ 0.437	\$ 0.163

* FFO and AFFO are non-GAAP financial measures of operating performance widely used by the real estate industry. Accordingly, FFO and AFFO should not be construed as an alternative to net income or cash flow from operating activities determined in accordance with GAAP.

FFO and AFFO have been calculated in accordance with the recommendations of RealPac, however, the method that is used by LREIT for calculating FFO and AFFO may differ from other issuers' methods and accordingly, may not be comparable with measures used by other issuers. The FFO and AFFO per unit amounts have been calculated on a basis consistent with that prescribed by GAAP for calculating earnings per unit.

Distributable Income

General

The stated policy of LREIT is to distribute cash to the Unitholders, on a monthly basis, in an amount which is approximately equal to 90% of the annual "Distributable income" of the Trust. Cash distributions may also be established at a specific level, as determined by the Trust and, as such, distributions may be greater than, or less than, distributable income.

Distributable income is a financial measurement which is commonly used to assess the cash distribution capabilities and cash flows of investment trusts and, as such, management believes that the disclosure of distributable income provides useful information to investors. Distributable income does not have any standardized meaning prescribed by GAAP and, therefore, the method that is used by LREIT for calculating distributable income may not be comparable to similar measures presented by other issuers. The most directly comparable GAAP measurement of the cash flows of LREIT is "cash from operating activities", as disclosed in the Consolidated Statement of Cash Flows in the financial statements. Accordingly, a reconciliation between cash from operating activities and distributable income is provided in the chart below.

Reconciliation Between Cash from Operating Activities and Distributable Income

	Year Ended December 31	
	2008	2007
Cash provided by operating activities, per Statement of Cash Flows	\$ 12,415,514	\$ 7,079,227
Changes in non-cash operating items	<u>(1,238,353)</u>	<u>(1,168,265)</u>
	11,177,161	5,910,962
Add (deduct):		
Tenant inducement and leasing expenses	592,552	105,479
Amortization of tenant inducement and leasing expenses	<u>(305,692)</u>	<u>(291,887)</u>
Distributable income	<u>\$ 11,464,021</u>	<u>\$ 5,724,554</u>
Per unit		
- Basic	\$ 0.656	\$ 0.328
- Diluted	\$ 0.592	\$ 0.321

Changes in non-cash operating items are excluded from LREIT's calculation of distributable income as non-cash operating items are subject to significant temporary fluctuations which are typically reversed over time, mainly due to timing differences in accounts receivable and accounts payable.

Tenant inducements and leasing expense fluctuate significantly throughout the year. Accordingly, the cash outlay for tenant inducements and leasing expenses is added-back for purposes of calculating distributable income, while amortization charges for cumulative tenant inducements and leasing expenses are deducted, as the amortization charges are considered to provide a more even distribution of leasing expenditures.

Distribution Variances

	Year Ended December 31	
	2008	2007
Distributions paid on trust units	\$ 8,104,253	\$ 9,336,147
Value of trust units issued under DRIP	<u>1,725,598</u>	<u>431,508</u>
Distributions per Statement of Equity	9,829,851	9,767,655
Distribution on LP units	<u>199,705</u>	<u>199,705</u>
Total distributions	<u>\$ 10,029,556</u>	<u>\$ 9,967,360</u>
Distributable income	<u>\$ 11,464,021</u>	<u>\$ 5,724,554</u>
Excess (shortfall) of distributable income over total distributions	<u>\$ 1,434,465</u>	<u>\$ (4,242,806)</u>
Cash provided by operating activities	<u>\$ 12,415,514</u>	<u>\$ 7,079,227</u>
Excess (shortfall) of cash provided by operating activities over total distributions	<u>\$ 2,385,958</u>	<u>\$ (2,888,133)</u>

Comparison to Distributable Income

During 2008, the distributable income of LREIT increased to a level which was in excess of the distributions of the Trust. In 2008, distributable income was equal to 117% of distributions, compared to 59% in 2007.

Comparison to Cash From Operating Activities

As disclosed in the preceding table, cash from operating activities exceeded distributions by \$2,385,958 or 26% during 2008, whereas in 2007, there was a shortfall between cash from operating activities and distributions of \$2,888,133 or 27%.

The significant improvement in the variance between total distributions, compared to distributable income and cash from operating activities in 2008, mainly reflects the extent to which the increase in net operating income exceeded the cash component of financing expense during the year.

The shortfall between distributions and cash from operating activities in 2007 was funded from financing activities, or more specifically, from mortgage loan proceeds.

As disclosed in the discussion of "working capital requirements" in the following sections of this report, the Trust also has additional funding requirements beyond the funding of distributions, including the funding of mortgage loan principal payments, property improvement costs, debenture interest payments and purchases under the normal course issuer bid.

Financing Activities

Summary

During 2008, the net cash flow provided by financing activities amounted to \$75,031,268. Financing activities consisted primarily of mortgage loan transactions, the repayment of convertible debentures, the purchase of units under the normal course issuer bid and distributions to the Unitholders.

Mortgage Loan Transactions

Mortgage Loan Proceeds

During 2008, mortgage loan proceeds amounted to \$132,885,288, consisting of the following:

- a first mortgage loan of \$22,781,500 which was obtained in May 2008 in regard to the acquisition of Millennium Village;
- \$7,739,731 of additional construction financing for Laird's Landing;
- a \$55 Million first mortgage loan which was obtained for Laird's Landing subsequent to the construction completion date. As noted below, the proceeds of the first mortgage loan were used to retire the cumulative amount of construction financing;
- \$21 Million of mortgage loan financing for the Siena Apartments;
- \$24.9 Million of additional interim loan financing;
- \$1,350,000 of second mortgage loan financing for Highland Tower; and
- \$114,057 of additional construction financing for Elgin Lodge.

Mortgage Loan Repayments

During 2008, mortgage loan principal repayments amounted to \$44,838,032, consisting of regular monthly repayments in the total amount of \$6,771,886 on the mortgage loan debt of the Trust, and the repayment of the construction loan for Laird's Landing in the amount of \$38,066,146.

Convertible Debentures

In March 2008, the outstanding balance of the Series D convertible debentures, in the amount of \$1,593,000, was retired.

Transaction Costs

During 2008, transaction costs amounted to \$1,340,590, of which \$1,259,903 pertained to mortgage loan financing and \$80,687 pertained to convertible debenture financing.

Purchase of Units

During 2008, LREIT purchased 456,200 units under its normal course issuer bid, at a weighted average price of \$3.90 per unit, representing a cash outflow of \$1,778,440.

Distributions

During 2008, the total cash outflow in regard to distributions amounted to \$8,303,958, including \$199,705 paid to the holder of the Class B Limited Partnership units. Distributions paid excludes the value of the units which were issued under DRIP.

Investing Activities

Summary

During 2008, the net cash outflow in regard to investment activities amounted to \$85,593,239. The investment activities consisted primarily of transactions related to new property and properties under development. Other cash outflows related to investing activities included improvements to income properties, deposits on potential acquisitions and changes in restricted cash.

New Property Acquisitions

During 2008, the total cash outflow in regard to new property acquisitions was \$46,865,000, comprised of the following amounts:

- a payment of \$25,500,000 in regard to the acquisition of the Siena Apartments, representing the purchase price of \$30 Million, less the vendor take-back mortgage of \$4 Million and deposits of \$500,000
- a partial payment of \$5 Million in regard to the acquisition of Parsons Landing; and
- a payment of \$16,365,000 in regard to Colony Square, representing the purchase price of \$37.8 Million, less deposits of \$950,000 and assumption of \$20,539,498 mortgage loan net of capital reserves.

The balance owing in regard to the acquisition of Millennium Village, in the amount of \$19,615,893, was also paid during 2008.

Properties Under Development

During 2008, the total cash outflow in regard to existing properties under development was \$8,248,758, comprised of the following amounts:

- total cash outflows of \$7,080,690 in regard to Laird's Landing, representing costs incurred prior to the reclassification of the apartment complex as an income-producing property; and
- \$1,168,068 of carrying costs in regard to Elgin Lodge and the Clarington Seniors Residence.

Construction of Income Properties

The total cash outlay to complete the construction of Laird's Landing, subsequent to the classification of the apartment complex as an income-producing property, was \$4,972,385.

Improvements to Income Properties

During 2008, the total cash outlay for improvements to Income Properties was \$3,565,986. The improvements consist of capital expenditures which were incurred during the normal course of operations, such as improvements to the income properties and grounds, as well as, common area upgrades and in-suite replacements, including appliances, carpeting and draperies.

Cash Flow Summary

A summary of the cash flow activities of the Trust during 2008 is provided below.

As disclosed in the chart, the net cash used in investment activities, excluding distributions, exceeded the net cash provided by financing activities by \$2,258,013, while cash from operating activities exceeded distributions paid by \$4,111,556. Distributions paid excludes the value of units issued under DRIP.

Overall, the net cash increase from operating, financing and investing activities during 2008 was \$1,853,543. After accounting for the opening bank indebtedness of \$1,623,651, LREIT completed 2008 with a cash balance of \$229,892.

Cash Flow Analysis (Note 1)

	Year Ended December 31, 2008
Financing Activities:	
Mortgage proceeds	\$ 132,885,288
Mortgage principal payments	(6,771,886)
Repayment of Series D debentures	(1,593,000)
Repayment of mortgage loans on refinancing	(38,066,146)
Normal course issuer bid	(1,778,440)
Transaction costs	(1,340,590)
Total financing	<u>83,335,226</u>
Investing Activities:	
Property acquisitions	(46,865,000)
Payment of acquisition cost payable	(19,615,893)
Improvements to income properties	(4,972,385)
Construction of income properties	(3,565,986)
Properties under development	(8,248,758)
Deposits	(1,010,000)
Restricted cash	(1,315,217)
Total investing	<u>(85,593,239)</u>
Net cash inflow (outflow) of investment capital	<u>(2,258,013)</u>
Operating activities	12,415,514
Cash distributions	<u>(8,303,958)</u>
Excess of cash from operating activities over distributions	<u>4,111,556</u>
Cash increase	1,853,543
Cash (bank indebtedness), beginning of year	<u>(1,623,651)</u>
Cash, end of year	<u><u>\$ 229,892</u></u>

Note 1 - GAAP Measurements

The preceding cash flow analysis represents the re-formatting of balances from the Consolidated Statement of Cash Flows in the financial statements in order to provide Unitholders with a direct depiction of the net inflow/outflow of investment capital, before considering the impact of operating activities and cash distributions. The components of financing activities, investing activities and operating activities, as disclosed in the analysis, agree to the Consolidated Statement of Cash Flows, with the exception of cash distributions which are excluded from financing activities and disclosed as a separate line item. The order of presentation of financing, investing and operating activities also differs from the Consolidated Statement of Cash Flows, in order to derive the subtotal entitled "net cash outflow of investment capital". Aside from the exclusion of cash distributions from financing activities and the subtotal entitled "net cash outflow of investment capital", the analysis consists entirely of GAAP measurements.

CAPITAL RESOURCES AND LIQUIDITY

Working Capital Requirements

As previously disclosed, cash from operating activities amounted to \$12,415,514 during 2008, while total distributions "paid" amounted to \$8,303,958, resulting in "excess" cash from operations of \$4,111,556. During 2008, regular monthly mortgage loan principal repayments amounted to \$6,771,886 and improvements to income properties amounted to \$3,565,986, representing a total of \$10,337,872. The regular monthly mortgage loan principal payments and property improvement costs of \$10,337,872 were partially funded from cash inflows from financing activities (i.e., mortgage loan proceeds) and the excess cash from operations.

In the absence of the additional mortgage loan financing in 2008, the cash from operating activities would not have been sufficient to fully fund distributions, given the funding needs in regard to regular monthly mortgage loan principal payments and property improvement costs.

Depending on the level of operating cash flows, additional financing may be required to meet all of the "non-operating" funding requirements of the Trust. Additional capital is also required on a periodic basis to fund the equity component of new property acquisitions and lump-sum convertible debenture repayments.

From a longer term perspective, the cash flow results for the fourth quarter of 2008 reflect management's belief of the cash flow generating potential of the property portfolio. During the fourth quarter of 2008, cash from operating activities amounted to \$5,761,651 or \$23,046,604 on an annualized basis, representing an amount which is sufficient to fully fund the total regular monthly mortgage loan principal payments, property improvement costs and cash distributions which were incurred in 2008.

Contractual Obligations

Property Acquisitions

As of December 31, 2008, the only outstanding commitment of LREIT in regard to property acquisitions was the \$48.2 Million balance owing in regard to Parsons Landing.

As a result of a delay in the funding of the mortgage loan financing for the property, the payment of the balance owing has been delayed. The date of payment of the balance owing has been extended to May 29, 2009, with interest. It is anticipated that the first mortgage loan financing for Parsons Landing will be completed in the second quarter of 2009.

Mortgage Loan Debt

A summary of the debt obligations of LREIT for 2009 and for each of the next five years and thereafter, is provided in the following chart:

Summary of Contractual Obligations - Long-term Debt

<u>Payments Due by Period</u>	<u>Total</u>	<u>1 Year</u>	<u>2 - 3 Years</u>	<u>4 - 5 Years</u>	<u>> 5 Years</u>
Regular mortgage loans	\$ 397,192,133	\$ 121,656,923	\$ 41,481,016	\$ 62,582,106	\$ 171,472,088
Interim mortgage loans	53,400,000	41,400,000	12,000,000	-	-
Vendor take-back mortgage loans	<u>5,600,000</u>	<u>1,600,000</u>	<u>4,000,000</u>	<u>-</u>	<u>-</u>
Total	<u>\$ 456,192,133</u>	<u>\$ 164,656,923</u>	<u>\$ 57,481,016</u>	<u>\$ 62,582,106</u>	<u>\$ 171,472,088</u>

The total amount due in year 1 is comprised of regular repayments of principal in the estimated amount of \$7,138,074; principal due of \$64,583,279 on loans which mature in 2009; and \$92,935,570 of principal due on demand loans, of which \$73,000,000 have terms that extend beyond 2009. Management intends to renew or refinance the principal amounts due under similar terms and conditions.

Convertible Debentures

Since the inception as a real estate investment trust, LREIT has issued seven series of convertible debentures, of which four have matured and been retired through conversion prior to maturity or repayment upon maturity, including the Series D debentures which were retired on March 16, 2008 with an outstanding balance of \$1,593,000. A summary of the net amount outstanding in regard to the three remaining series of convertible debentures is provided in the following chart.

<u>Issue Date/Maturity Date</u>	<u>Series</u>	<u>Amount Issued</u>	<u>Net Amount Outstanding December 31, 2008</u>
Feb. 17/05/Feb. 17/10	E	\$ 12,000,000	\$ 11,950,000
Mar. 10/06/Mar. 11/11	F	13,680,000	13,680,000
Dec. 8/06/Dec. 31/11	G	<u>25,732,000</u>	<u>25,732,000</u>
Face Value		<u>\$ 51,412,000</u>	<u>\$ 51,362,000</u>

Improvements to Existing Properties

During 2009, property improvement costs are expected to be approximately \$2 Million.

Operating Line of Credit

As previously disclosed, LREIT has a revolving line of credit in the maximum amount of \$5 Million. The Line of credit bears interest at prime and is repayable on demand.

As of December 31, 2008, \$1,555,000 was available to the Trust under the line of credit. The amount available is net of an amount used to secure a letter of credit of \$125,000.

Normal Course Issuer Bid

As previously noted in this report, LREIT purchased 99,507 units under the normal course issuer bid in January 2009 at a cost of \$275,758. Due to the cash constraints of the Trust, it is anticipated that there will be a limited number of additional purchases under the normal course issuer bid in 2009. The Trust is not required to purchase any units under the normal course issuer bid.

Sources of Capital

Existing Cash

As of December 31, 2008, the cash balance of LREIT was \$3,549,892, excluding the amount drawn on the line of credit of \$3,320,000. The working capital balance of the Trust, excluding accrued liabilities for property acquisitions or properties under development, was approximately \$3.9 Million as of December 31, 2008.

Cash from Operating Activities

During 2008, cash from operating activities amounted to \$12,415,514. It was previously anticipated that, in 2009, cash from operating activities would increase to a level that would be sufficient to cover the "non-operating" funding requirements of the Trust. The increase in cash from operating activities was expected to be derived from the operations of the 2008 property acquisitions for a full year in 2009, offset, to a minor degree, by modest operating losses on the Clarington Seniors Residence and the Elgin Lodge expansion. During the fourth quarter of 2008, cash from operating activities amounted to \$5,761,651 or \$23,046,604 on an annualized basis.

The recent downturn in the multi-family residential rental market in Fort McMurray has negatively impacted the cash flow projections of the Trust. Although it is not possible to predict the length or the severity of the economic slowdown in Fort McMurray, it is anticipated that cash from operating activities will be significantly lower in 2009, compared to 2008.

As a result of the projected reduction in operating cash flow, it is necessary for LREIT to reduce the amount of its annual distribution. Specifically, LREIT has established a total distribution of \$0.27 per unit for 2009, compared to a total of \$0.56 per unit for 2008.

The reduction in the total distribution for 2009 is being implemented in conjunction with a change in the distribution policy from monthly distributions to quarterly distributions, effective immediately. Specifically, LREIT is implementing a change from a monthly distribution policy to a quarterly distribution policy, whereby quarterly distributions of \$0.06 per unit (\$0.24 per unit annualized) would be payable on July 15, October 15 and December 31 to the Unitholders of record as of June 30, September 30 and December 31, respectively. The three quarterly distributions in the combined amount of \$0.18 per unit, plus the distributions of \$0.04667 per unit in January 2009 and February 2009 comprise the total projected distribution of \$0.27 per unit. A distribution will not be paid in April 2009.

Divestiture Program

During the next year, LREIT will also undertake a divestiture program, for \$150 Million of assets at appraised values. The proceeds of sale to be used for the repayment of higher cost and shorter term debt of LREIT. The objective of the divestiture program is to reduce total debt, including convertible debenture debt, by a minimum of 25%, and to reduce the total debt to appraised value ratio to approximately 60%.

Mortgage Loan Financing

After considering the decrease in distributions and the impact of the divestiture program, cash from operations is expected to be sufficient to meet the "non-operating" funding requirements of LREIT during 2009. As opportunities arise, first mortgage loans may be upward refinanced at maturity in order to raise additional capital to supplement the cash generated from operating activities.

Management of LREIT expects that the mortgage loan financing for Parsons Landing will be obtained and funded in the second quarter of 2009. The financing is expected to be sufficient to fund the entire amount of the balance owing, including accrued interest and the GST payable.

Debenture and/or Trust Unit Offerings

From a longer term perspective, LREIT has the capability of pursuing additional debenture or trust unit offerings as a source of investment capital. LREIT may also issue trust units to vendors as consideration for real property acquisitions.

RELATED PARTY TRANSACTIONS

Shelter Canadian Properties Limited ("Shelter Canadian")

Shelter Canadian provides administrative and asset management services to LREIT, pursuant to the terms of a Services Agreement. The Services Agreement provides for the remuneration of Shelter Canadian to be established at a level which is commensurate with customary comparable market asset management fees, subject to the discretion of the Governance, Compensation and Nominating Committee of the Board of Trustees.

Commencing January 1, 2006, the Committee approved a service fee equal to 0.3% of the gross book value of the total assets of the Trust. The gross book value of the total assets of the Trust is defined as the total assets, as disclosed on the most recently issued financial statements, excluding cash and accumulated amortization. Payment of the fee occurs on a monthly basis, on the last day of each month. The current term of the Services Agreement expires on June 30, 2009.

Mr. Arni Thorsteinson, Chief Executive Officer of LREIT and a Trustee, is a Director and President of Shelter Canadian and the President of the parent corporation of Shelter Canadian, 2668921 Manitoba Ltd. As of February 2007, the Governance, Compensation and Nominating Committee is comprised of all of the independent Trustees of LREIT. Prior to February 2007, Mr. Thorsteinson was a member of the Governance and Compensation Committee and, as such, Mr. Thorsteinson abstained from all discussions and voting in regard to the approval of the service fee.

Shelter Canadian is also the Property Manager for LREIT, pursuant to the Property Management Agreement. Shelter Canadian has a direct involvement in the management of all of the income properties in the portfolio of LREIT and acts as the Property Manager for all of the properties, except for Siena Apartments and the seniors' housing complexes, which are managed by third party managers who specialize in seniors' housing. The current term of the Management Agreement expires on August 30, 2012.

Development Agreement for Laird's Landing

The construction and lease-up of the Laird's Landing apartment complex was substantially completed as of June 1, 2008. The construction of the property was completed pursuant to a development agreement with Shelter Canadian. Pursuant to the development agreement, Shelter Canadian agreed to:

- (1) develop the Project for a total cost not to exceed \$57.75 Million, inclusive of the purchase price of the land. (The total cost of the project was \$53.6 Million, including land costs.)
- (ii) arrange and guarantee construction financing in the approximate amount of \$45 Million and permanent financing after completion of construction (a first mortgage demand loan of \$55 Million was arranged in September, 2008); and
- (iii) provide all development and construction supervision services for the Project.

The agreement provided for Shelter Canadian to earn a development fee from LREIT in the maximum amount of \$1,000,000, in consideration for its services under the development agreement, representing approximately 1.73% of the total estimated Project cost. The fee of \$1,000,000 was fully paid as of June 30, 2008.

The development agreement was approved by the independent trustees of LREIT and Mr. Thorsteinson abstained from voting on the resolution approving the transaction.

REVENUE/INCOME AND OTHER COMMITMENTS

Lakewood Manor

The acquisition of Lakewood Manor was completed by LREIT, effective July 1, 2007. All of the units at the property are leased and occupied by a major oil sands company, pursuant to a three year lease agreement, under which the lessee is also responsible for all property operating costs. The net operating income of the property is approximately \$4.8 Million per annum, representing the amount of gross rental revenue.

The agreement also provides the oil sands company with an option to extend the lease for an additional two years, at a 10% increase in the annual absolute net operating income. In addition, the agreement provides the lessee with a three year purchase option to acquire all of the 64 townhouse units at a price of \$26,873,600 to June 30, 2009 and \$27,667,200 to June 30, 2010.

Siena Apartments

The acquisition of Siena Apartments was completed by LREIT, effective July 2, 2008. All of the units at the property are leased and occupied by a major oil sands company, pursuant to a lease agreement expiring May 1, 2012, under which the lessee is also responsible for all property operating costs. The net operating income of the property is approximately \$2.2 Million per annum, representing the amount of gross rental revenue.

The agreement also provides the oil sands company with an option to extend the lease for an additional five years at current market rates at that time.

Elgin Lodge

In conjunction with the acquisition of Elgin Lodge in June 2006, LREIT retained Kingsway Arms Management Services Inc. ("Kingsway") to manage the property for a ten year term, expiring on May 31, 2016. Kingsway is an Ontario-based company, which acquires, manages and develops retirement homes, catering principally to the independent and assisted living segments. Kingsway currently manages a portfolio of nine properties, totaling 850 suites located across Ontario.

As previously disclosed in this report, a 60 suite expansion was completed at Elgin Lodge during 2007. During the five year period from June 1, 2006, Kingsway is entitled to a one-time payment equal to 50% of the amount by which the appraised value of the expanded property exceeds the total of the cost of the property to LREIT, including the cost of the expansion and the unpaid portion of a 12% annual return on the LREIT equity investment. Consideration recorded at December 31, 2008, of \$314,869, which increases the cost of the building, is included in accounts payable and accrued liabilities.

The Clarington Seniors Residence

LREIT has also retained Kingsway to manage The Clarington Seniors Residence for a ten-year term, expiring on February 12, 2017. During the five year period after the "lease-up" date, Kingsway is entitled to a one-time payment equal to 50% of the amount by which the appraised value of the property exceeds the total of the original acquisition cost to LREIT and the unpaid portion of a 8% annual return on the LREIT equity investment. Consideration recorded at December 31, 2008, of \$313,951, which increases the cost of the building, is included in accounts payable and accrued liabilities.

Parsons Landing

The funding of the mortgage financing for Parsons Landing has been delayed and, as a result, the vendor has agreed to extend the deadline for payment of the balance owing until May 29, 2009 and to accept partial payment on account of interest of \$600,000, payable in two installments of \$300,000 in March and April of 2009. The payment extension is conditional upon LREIT obtaining a commitment for mortgage financing of \$45,000,000 by April 15, 2009. In the event that a financing commitment is not received by April 15, 2009, the vendor will be permitted to list the property for sale. Depending on the price, the sale may result in the \$15,000,000 paid to the vendor to date, or a portion thereof, being lost.

CHANGES IN ACCOUNTING POLICIES

New Accounting Standards - Adopted January 1, 2008

On January 1, 2008, the Trust adopted CICA Handbook Section 1535 - Capital Disclosures, Section 3862 - Financial Instruments - Disclosures and Section 3863 - Financial Instruments - Presentation. Section 1535 requires the Trust to disclose information that enables users of its financial statements to evaluate the Trust's objectives, policies and processes for managing capital. Sections 3862 and 3863 replace the existing Section 3861, Financial Instruments - Disclosure and Presentation. These new sections revise and enhance disclosure requirements and carry forward unchanged existing presentation requirements. These new sections require disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. The new standards do not have any impact on the classification or measurement of financial instruments.

Future Changes to Significant Accounting Policies

Goodwill and intangible assets

In February 2008, the CICA issued a new Handbook Section 3064, "Goodwill and Intangible Assets". This new section replaces Section 3062, "Goodwill and Intangible Assets", and establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. Handbook Section 1000, Financial Statement Concepts, was also amended to provide consistency with this new standard. The new and amended standards will be effective for the REIT's 2009 fiscal year, and will be adopted on a retroactive basis with restatement of the prior years.

The new policy will not have any impact on the consolidated financial statements.

International Financial Reporting Standards

The CICA Accounting Standards Board has adopted a strategic plan for the direction of accounting standards in Canada. As part of the plan, accounting standards for public companies will be required to converge with International Financial Reporting Standards for fiscal years beginning on or after January 1, 2011 with comparative figures presented on the same basis. The International Financial Reporting Standards will replace Canada's current GAAP for public companies.

Management is currently in the process of evaluating the potential impact of the International Financial Reporting Standards to the consolidated financial statements. This will be an ongoing process as new standards and recommendations are issued by the International Accounting Standards Board and the CICA. The consolidated financial performance and financial position, as disclosed in the current GAAP financial statements, may be significantly different when presented in accordance with International Financial Reporting Standards.

The CICA has provided public companies with the option to early adopt International Financial Reporting Standards, effective January 1, 2009. The Trust does not intend to early adopt these standards on January 1, 2009.

Business Combinations

CICA Handbook Section 1582 - Business Combinations will apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. CICA Handbook Sections 1601 - Consolidations and 1602 - Non-Controlling Interests will be effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier adoption of these sections is permitted as of the beginning of a fiscal year. All three sections must be adopted concurrently. These sections replace the former CICA Handbook Sections 1581 - Business Combinations and 1600 - Consolidated Financial Statements. CICA Handbook Section 1601 establishes standards for the preparation of consolidated financial statements. CICA Handbook Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination.

OPERATING RISKS AND UNCERTAINTIES

An investment in units of LREIT encompasses the risks which are inherent in the ownership and operation of a portfolio of residential and commercial properties, as well as the normal risks which are associated with an investment in a real estate investment trust. For a summary of certain additional key risks relating to LREIT, see the Annual Information Form, which is available at www.sedar.com.

The key risks include the following:

Real Property Ownership

The properties of LREIT are subject to the normal risks common to real property ownership and operation, including the risk of a reduced demand due to changes in general economic conditions, local real estate markets, competition from other available premises and various other factors.

The properties of LREIT generate income through rent payments made by the tenants of the properties. Upon the expiry of any lease, there can be no assurance that the lease will be renewed or the tenant replaced. The terms of any subsequent lease may be less favourable than the existing lease. Leasing results are affected by a number of factors, including location of the property and, in particular, the level of supply and demand in the local rental market.

Certain significant expenditures, including property taxes, utility payments, maintenance costs, mortgage payments, insurance costs and related charges must be made throughout the period of ownership of real property regardless of whether the property is producing any income. If LREIT were unable to meet mortgage payments on any property, losses could be sustained as a result of the mortgagee's exercise of its rights of foreclosure or sale.

Real property investments tend to be relatively illiquid, with the degree of liquidity generally fluctuating in relation to demand for the perceived desirability of such investments. Such illiquidity may tend to limit LREIT's ability to vary its portfolio promptly in response to changing economic or investment conditions. If LREIT were to be required to liquidate its real property investments, the proceeds to LREIT might be significantly less than the aggregate carrying value of its properties.

Financing

The ability of LREIT to raise additional capital for operating or investing activities is subject to uncertainty. Factors which could impair the ability of LREIT to raise additional capital include a continued downturn in general economic conditions, a more restrictive capital market, a change in legislation and numerous other factors beyond the control of LREIT.

Payment of Cash Distributions

A return on an investment in units is not comparable to the return on an investment in a fixed-income security. The recovery of the initial investment in units is at risk and the return on an investment in units is based on many performance assumptions. The ability of LREIT to pay distributions in excess of its Distributable Income is dependent upon the level of cash reserves, the debt covenants and obligations of the Trust, the working capital requirements of the Trust and the future capital requirements of the Trust. Cash distributions may be reduced or suspended at any time. In addition, the market value of the units may decline if LREIT is unable to provide a satisfactory return to Unitholders.

Public Market Risk

It is not possible to predict the price at which units will trade in the future and there can be no assurance that an active trading market for the units will be sustained. The units will not necessarily trade at values determined solely by reference to the value of the properties of LREIT. Accordingly, the units may trade at a premium or a discount to the value implied by the value of the properties of LREIT. The market price for the units may be affected by changes in general market conditions, fluctuations in the markets for equity securities and numerous other factors beyond the control of LREIT.

Closing of Proposed Acquisitions

There can be no assurance that LREIT will complete the acquisition described herein on the basis described herein or on the expected closing dates, if at all. The successful growth of LREIT will depend on the ability of Management to complete the acquisition and successfully integrate the acquired properties and identify opportunities for future property acquisitions. The ability of Management to generate growth from property acquisitions may be affected by elevated acquisition costs, funding of the acquisitions, unexpected liabilities with regards to the properties and other problems related to the integration of the properties. Management's failure to successfully grow through future property acquisitions could adversely affect LREIT's financial condition, net income from operations and its ability to generate cash available for distribution.

As previously disclosed, there is a risk that financing arrangements for Parsons Landing will not be completed within a satisfactory time frame and that the property would be listed for sale.

Concentration of LREIT's Portfolio in One Market

The property portfolio of LREIT has significant exposure to the Fort McMurray, Alberta market. As of December 31, 2008, there were 44 properties in the real estate portfolio of LREIT, including four commercial properties and 40 residential properties, comprising 3,913 rental units. 13 of the residential properties, comprising a total of 1,167 suites, or 30% of the total residential suites, are located in Fort McMurray. The 13 properties have an aggregate acquisition price of \$336.8 Million, which represents approximately 57% of the total aggregate purchase price of the real estate portfolio.

The 13 properties in Fort McMurray accounted for 50.7% of the total revenue of LREIT during 2008 and 59.7% of the total operating income.

Oil Sands Industry

As disclosed above, LREIT has a high concentration of properties in the Fort McMurray, Alberta market and employees from the oil sands industry represent the primary tenant base of the Fort McMurray portfolio, however, LREIT also has two properties in Fort McMurray which are 100% leased to major oil sands companies, under a single lease agreement, as follows:

- Lakewood Manor - all units 100% leased under a three year lease agreement, expiring on June 30, 2010, with the option of an extension for two years with a 10% rental rate increase; and
- Siena Apartments - all units 100% leased under a lease agreement, expiring on May 1, 2012, with the option of an extension for five years at current market rates at that time.

As a result of the decline in global economic conditions and the impact of reduced oil prices on the oil sands industry, there is an increased risk of potential lease defaults for suites which are leased to oil sands companies or to the employees of oil sands companies.

Changes to Tax Treatment of Trusts

LREIT currently qualifies as a mutual fund trust for income tax purposes. As required by its Declaration of Trust, LREIT is required to distribute an amount equal to not less than all of its taxable income to its Unitholders and to deduct these distributions for income tax purposes.

On June 22, 2007, new legislation relating to, among other things, the federal income taxation of publicly traded income trusts (the "New SIFT Rules") was enacted. Under the New SIFT Rules, certain distributions from a "specified investment flow-through" trust (a "SIFT") will no longer be deductible in computing a SIFT's taxable income, and a SIFT will be subject to tax on such distributions at a rate that is substantially equivalent to the general tax rate applicable to a Canadian corporation. Distribution of income of SIFT's received by a Unitholder that are not deductible to the SIFT will be treated as dividends payable to the Unitholders, however, distributions paid by a SIFT as a return of capital will generally not be subject to the tax.

The New SIFT Rules provide that a SIFT which was publicly listed prior to November 1, 2006 (an "Existing Trust") will become subject to the tax on distributions commencing in the 2011 taxation year. However, an Existing Trust may become subject to this tax prior to 2011 if its equity capital increases beyond certain limits measured against the market capitalization of the Existing Trust at the close of trading on October 31, 2006. Based on its October 31, 2006 market capitalization, LREIT may increase its equity capital by \$50 Million for each of the years ending December 31, 2008, December 31, 2009 and December 31, 2010 (the "Safe Harbour Limit"). To date, LREIT's equity capital has not increased beyond the Safe Harbour Limit.

The New SIFT Rules do not apply to a "real estate investment trust" (a "Qualifying REIT") that meets prescribed conditions relating to the nature of its income and investments (the "REIT Conditions"). In the opinion of management, the Trust does not currently satisfy the REIT Conditions. Accordingly, LREIT is subject to the New SIFT Rules and, subject to earlier application if it increases its equity capital beyond its Safe Harbour Limit, LREIT will be subject to the tax on distributions commencing in 2011. Prior to 2011, LREIT will consider its alternatives, including restructuring its affairs to qualify as a Qualifying REIT, however, no assurances can be given that any reorganization can or will be implemented before 2011, or that any such reorganization, if implemented, would not result in material costs or other adverse consequences to LREIT and its Unitholders. In addition, no assurance can be given that LREIT's equity capital will not increase beyond the Safe Harbour Limit prior to 2011.

Legal Claims

In the normal course of operations, the Trust will become subject to a variety of legal and other claims. Management and legal counsel evaluate all claims on their apparent merits, and accrue management's best estimate of the estimated costs to satisfy such claims. Although the outcome of legal and other claims are not reasonably determinable, management believes that any such outcome will not be material.

Relationship with Shelter Canadian Properties Limited

The financial performance of LREIT will depend in part on the performance of Shelter Canadian in providing administrative and asset management services to the Trust, pursuant to the Services Agreement.

Reliance on Key Personnel

The success of LREIT is highly dependent on the services of certain management personnel, including Arni Thorsteinson. The loss of the services of such personnel could have an adverse effect on LREIT.

Other

Other risks and uncertainties are more fully explained in the other regulatory filings of LREIT, including the Annual Information Form.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the consolidated financial statements of LREIT, in accordance with Canadian generally accepted accounting principles (GAAP), requires management to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. The estimates are based on historical experience and on other assumptions that are believed to be reasonable under the circumstances. Under different assumptions or conditions, the actual results may differ, potentially materially, from the estimated amounts. Many of the conditions impacting the assumptions and estimates are beyond the control of management. The estimates and assumptions are evaluated on a periodic basis.

Financial statement items which encompass estimates include the following:

- allocation of the cost of property acquisition: a portion of the acquisition cost of an income property is allocated to tenant origination costs associated with in-place leases and the cost of tenant relationships, lease origination costs above market leases and below market leases. The amount allocated to the above is based on the estimated fair market value of each variable. The allocated amounts are of significance, as the costs are amortized over a relatively short time frame (i.e., the term of the respective tenant leases) in comparison to the amount allocated to buildings and equipment;
- amortization of the building component of Income Properties: a portion of the purchase price of an income property is allocated to "building" based on the estimated value of the building on an "as if vacant" basis. Amortization expense is based on the estimated useful life of the building. The estimated useful life of the building may vary and could result in a different amount of amortization charged to income;

- amortization of property improvements: expenditures relating to improvements to income properties are capitalized to the cost of income properties and amortized for a period of five to 25 years, based on the estimated useful life of the improvements. The estimated useful life of improvements may vary and could result in a different amount of amortization charged to income;
- unit-based compensation expense: unit-based compensation expense is based on the estimated fair value of the applicable options using the Black-Scholes option pricing method;
- the determination of the amount of temporary differences, the timing of reversal and the tax rate to be used in calculating future income tax assets and liabilities; and
- the allocation of convertible debentures between debt and equity based on the estimated fair value of the debt using an estimated cost of borrowing.

The estimates which were used for financial statement reporting purposes, for the above noted items, are not expected to change from period to period.

TAXATION

Taxation of LREIT

LREIT qualifies as a mutual fund trust for income tax purposes. Subject to the New SIFT Rules, LREIT is generally subject to tax in Canada under the Income Tax Act (the "Tax Act") in respect to its taxable income each year, except to the extent that such taxable income is paid or deemed to be payable to Unitholders and deducted by LREIT for tax purposes. Pursuant to the Declaration of Trust of LREIT, the Trustees distribute or designate all taxable income directly earned by LREIT to the Unitholders of the Trust in order to ensure that LREIT will not be subject to income tax under Part I of the Tax Act.

Under the New SIFT Rules, if LREIT does not meet the REIT Conditions to become a Qualifying REIT resulting in the tax on distributions commencing to apply to LREIT in 2011 (or earlier if LREIT increases its equity capital beyond its Safe Harbour Limit), certain distributions from LREIT will no longer be deductible in computing its taxable income, and it will be subject to tax on such distributions at a rate that is substantively equivalent to the general tax rate applicable to a Canadian corporation. However, distributions paid as a return of capital will generally not be subject to the tax.

Taxation of Unitholders

The Declaration of Trust generally requires LREIT to claim the maximum amount of capital cost allowance for purposes of computing its income for tax purposes. Subject to the New SIFT Rules, a Unitholder is required to include, in computing income for tax purposes each year, the portion of the amount of net income and net taxable capital gains of LREIT paid or payable to the Unitholder in the year. Distributions in excess of the taxable income of LREIT for the year which are allocated to a Unitholder are not included in computing the taxable income of the Unitholder. However, the adjusted cost base of the units which are held by a Unitholder will generally be reduced by the amount of distributions not included in income.

The cash distributions which have been paid to the Unitholders since the inception of LREIT as a real estate investment trust in September 2002, have exceeded the income of LREIT, as calculated for income tax purposes. All of the distributions, which have been paid by LREIT from September 2002 to December 31, 2008, have represented a reduction in adjusted cost base of the units.

Under the New SIFT Rules, should they become applicable to LREIT as set out above, certain distributions from LREIT which would otherwise have been ordinary income will be characterized as dividends in addition to being subject to tax in LREIT at rates similar to the combined federal and provincial corporate tax rates. Distributions to Canadian resident individuals will be deemed to be "eligible dividends", qualifying for the enhanced dividend tax credit.

Upon the disposition or deemed disposition by a Unitholder of a unit, a capital gain (or a capital loss) will generally be realized to the extent that the net proceeds of disposition of the unit exceed (or are exceeded by) the adjusted cost base of the unit. Currently, only 50% of a capital gain ("taxable capital gain") must be included in computing a Unitholders' income and 50% of a capital loss (an "allowable capital loss") may be deducted against taxable capital gains.

INTERNAL CONTROLS OVER FINANCIAL REPORTING

For the financial year ended December 31, 2008, the Chief Executive Officer and the Chief Financial Officer (the "Certifying Officers"), together with other members of management, have evaluated the design and operational effectiveness of LREIT's disclosure controls and procedures, as defined in Multilateral Instruments 52-109. The Certifying Officers have concluded that the disclosure controls and procedures are designed to ensure that information is accumulated and communicated to management, to allow timely decisions regarding required disclosures.

The internal controls over financial reporting are designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian Generally Accepted Accounting Principles. The Certifying Officers, together with other members of management, have evaluated and concluded that the design and operation of LREIT's internal controls over financial reporting are effective for the financial year ended December 31, 2008.

No changes were made to the design of the internal controls over financial reporting during the year ended December 31, 2008 that have materially affected, or are reasonably likely to materially affect, the effectiveness of the internal control system.

Readers are cautioned, however, that a control system can only provide reasonable, not absolute, assurance that the objectives of the control system are achieved. Due to the inherent limitations in all control systems, an evaluation of controls cannot provide absolute assurance that all control issues, including instances of fraud, if any, have been detected. Inherent limitations include the possibility that the assumptions and judgments of management could ultimately prove to be incorrect under varying conditions and circumstances; or that isolated errors could prove to have a significant impact on the reliability of information.

Additionally, controls may be circumvented by the unauthorized acts of individuals, by collusion of two or more people, or by management override. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and it is not possible to provide complete assurance that a control system will succeed in achieving its stated goals under all potential future conditions.

ADDITIONAL INFORMATION

Additional information relating to LREIT, including the Annual Information Form, is available on the SEDAR website at www.sedar.com. SEDAR acts as a facilitator for the electronic filing of securities information, as required by the securities regulatory agencies in Canada.

APPROVAL BY TRUSTEES

The content of the 2008 Annual Report of Lanesborough Real Estate Investment Trust, including Schedule I, and the delivery of the report to the Unitholders has been approved by the Trustees.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST
March 24, 2009

LANESBOROUGH REAL ESTATE INVESTMENT TRUST MANAGEMENT'S DISCUSSION AND ANALYSIS - 2008

SCHEDULE I

Real Estate Portfolio as of December 31, 2008

Property Portfolio - December 31, 2008

Property	Location	Purchase Price	Acquisition Date	Suites/ Leasable Area - Sq. Ft.	Occupancy December 31 2008
RESIDENTIAL					
Manitoba					
Highland Tower (1)	Thompson	\$ 5,700,000	January 2005	77	97 %
Chancellor Gate	Winnipeg	6,750,000	August 2005	48	94 %
Colony Square	Winnipeg	29,907,700	October 2008	428	96 %
Willowdale Gardens	Brandon	4,326,000	January 2006	88	98 %
Saskatchewan					
Borden Estates	Prince Albert	5,315,000	February 2005	144	87 %
Cedar Village	Prince Albert	2,700,000	February 2005	72	93 %
Carlton Manor	Prince Albert	410,000	February 2005	19	87 %
Riverside Apartments	Prince Albert	265,000	February 2005	12	96 %
MGM Apartments	Prince Albert	650,000	February 2005	28	45 %
Marquis Towers	Prince Albert	6,200,000	August 2005	129	99 %
Riverside Terrace (2)	Saskatoon	24,000,000	July 2005	181	100 %
Village West	Saskatoon	5,113,800	June 2006	100	98 %
Sir Robert Borden Place	Saskatoon	5,600,000	May 2007	113	98 %
Chateau St. Michael's (2)	Moose Jaw	7,600,000	June 2006	93	99 %
Woodlily Courts	Moose Jaw	3,700,000	June 2006	102	99 %
Alberta					
Nova Villa	Edmonton	5,400,000	May 2004	61	95 %
Nova Manor	Edmonton	2,615,000	May 2004	32	96 %
Nova Ridge Estates	Spruce Grove	8,800,000	July 2004	102	98 %
Norglen Terrace	Peace River	2,500,000	October 2004	72	99 %
Broadview Meadows	Sherwood Park	6,790,000	January 2006	93	99 %
Nelson Ridge Estates	Fort McMurray	40,575,000	April 2005	225	95 %
Gannet Place	Fort McMurray	6,873,700	June 2006	37	95 %
Lunar Apartments	Fort McMurray	4,457,100	June 2006	24	96 %
Parkland Apartments	Fort McMurray	2,230,200	June 2006	12	99 %
Skyview Apartments	Fort McMurray	5,385,800	June 2006	29	97 %
Snowbird Manor	Fort McMurray	6,314,500	June 2006	34	99 %
Whimbrel Terrace	Fort McMurray	6,873,700	June 2006	37	97 %
Laird's Landing	Fort McMurray	51,350,000	August 2006	189	97 %
Woodland Park	Fort McMurray	37,865,000	March 2007	107	94 %
Lakewood Manor	Fort McMurray	59,900,000	July 2007	175	100 %
Millennium Village	Fort McMurray	24,220,000	November 2007	72	94 %
Parsons Landing (3)	Fort McMurray	60,733,000	September 2008	160	93 %
Siena Apartments	Fort McMurray	30,000,000	July 2008	66	100 %
Westhaven Manor	Edson	4,050,000	May 2007	48	96 %
Northwest Territories					
Beck Court	Yellowknife	14,300,000	April 2004	120	100 %
Three Lakes Village	Yellowknife	10,900,000	May 2005	50	99 %
Nova Court (4)	Yellowknife	15,000,000	March 2007	106	100 %
Ontario					
Elgin Lodge (2)(5)	Port Elgin	18,067,000	June 2006	124	66 %
Clarington Seniors Residence (2)(6)	Bowmanville	22,400,000	February 2007	121	49 %
British Columbia					
Greenwood Gardens	Surrey	10,950,000	April 2004	183	95 %
Total - Residential		\$ 566,787,500	Total suites	3,913	

Property Portfolio - December 31, 2008 (continued)

Property	Location	Purchase Price	Acquisition Date	Suites/ Leasable Area - Sq. Ft.	Occupancy December 31 2008
Total - Residential		\$ 566,787,500	Total suites	3,913	
COMMERCIAL					
Retail and Office					
Kenaston (1)	Winnipeg, MB	12,656,200	April 2002	103,209	88 %
Mclvor Mall	Winnipeg, MB	6,700,000	February 2004	65,283	95 %
Colony Square	Winnipeg, MB	7,931,600	October 2008	83,190	92 %
		<u>27,287,800</u>		<u>251,682</u>	
Light Industrial					
156 / 204 East Lake Blvd. (7)	Aidrie, AB	1,600,000	June 2003	39,936	- %
Purolator	Burlington, ON	1,200,000	September 2003	16,117	100 %
		<u>2,800,000</u>		<u>56,053</u>	
Total - Commercial		30,087,800	Total leasable area	307,735	
Total real estate portfolio		\$ 596,875,300			

Notes to the Property Portfolio:

- (1) Includes the cost of major renovations and asset additions.
- (2) Seniors housing complex.
- (3) LREIT took possession of Parsons Landing on September 1, 2008. LREIT is obligated to pay the balance of the purchase price in the second quarter of 2009. See "Property Acquisitions - Parsons Landing" above.
- (4) Property includes 8,400 square feet of commercial space.
- (5) Costs in regard to the expansion of \$9,767,000 are classified as "properties under development".
- (6) Property is classified as "properties under development".
- (7) Formerly MAAX Warehouse.

MANAGEMENT'S RESPONSIBILITY

The consolidated financial statements and management's discussion and analysis contained in the annual report are the responsibility of the management of Lanesborough Real Estate Investment Trust. To fulfill this responsibility, management maintains systems of internal control which are designed to give reasonable assurance that transactions are authorized and properly recorded, assets are safeguarded and financial records are properly maintained to provide reliable financial information for the preparation of the consolidated financial and other financial reports. The consolidated financial statements have been prepared in conformity with Canadian generally accepted accounting principles and, where appropriate, reflect estimates based on management's best judgment in the circumstances.

The financial statements have been reviewed and approved by the Board of Trustees and by the Audit Committee, which is comprised of independent Trustees. The Audit Committee meets regularly with management and the auditors. The auditors have full and direct access to the Audit Committee.

Meyers Norris Penny LLP, the independent chartered accountants, were appointed by the Unitholders and are engaged to audit the consolidated financial statements in accordance with generally accepted auditing standards and provide an independent auditor's opinion.

"Arni C. Thorsteinson"

"Kenneth J. Dando"

Arni C. Thorsteinson
Chief Executive Officer

Kenneth J. Dando
Chief Financial Officer

March 24, 2009

To the Unitholders of Lanesborough Real Estate Investment Trust:

We have audited the consolidated balance sheets of Lanesborough Real Estate Investment Trust as at December 31, 2008 and 2007 and the consolidated statements of equity, loss and comprehensive loss and cash flows for the years then ended. These financial statements are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Trust as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Winnipeg, Manitoba

March 24, 2009

Meyer Norris Penny LLP

Chartered Accountants

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

CONSOLIDATED BALANCE SHEETS

	<u>December 31 2008</u>	<u>December 31 2007</u>
Assets		
Income properties (Note 4)	\$554,090,286	\$375,796,299
Properties under development (Note 5)	35,957,774	80,228,769
Mortgage loan receivable (Note 6)	-	10,000,000
Cash (Note 12)	229,892	-
Other assets (Note 7)	8,480,947	6,410,441
Future income taxes (Note 11)	<u>3,429,431</u>	<u>3,763,761</u>
	<u>\$602,188,330</u>	<u>\$476,199,270</u>
Liabilities and Equity		
Mortgage loans payable (Note 8)	\$453,927,161	\$341,334,043
Convertible debentures (Note 9)	42,427,966	41,036,253
Accounts payable and accrued liabilities (Note 10)	63,312,264	31,339,325
Bank indebtedness (Note 12)	-	1,623,651
Future income taxes (Note 11)	<u>3,518,197</u>	<u>2,617,905</u>
	563,185,588	417,951,177
Non-controlling interest (Note 13)	1,573,258	1,685,103
Equity	<u>37,429,484</u>	<u>56,562,990</u>
	<u>\$602,188,330</u>	<u>\$476,199,270</u>

Approved by the Board of Trustees

"Charles Loewen"

"Cheryl Barker"

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF EQUITY

Year Ended December 31, 2008:

	Units	Cumulative Loss	Cumulative Distributions	Equity Component of Debentures	Total
Equity, December 31, 2007	\$ 79,124,607	\$ (8,322,299)	\$ (27,666,613)	\$ 13,427,295	\$ 56,562,990
Maturity of Series D debentures	322,658	-	-	(322,658)	-
Units purchased under normal course issuer bid	(1,778,440)	-	-	-	(1,778,440)
Issue costs	(111,802)	-	-	-	(111,802)
Unit-based compensation	391,517	-	-	-	391,517
Units issued on distribution reinvestment plan	1,802,126	-	-	-	1,802,126
Loss and comprehensive loss	-	(9,607,056)	-	-	(9,607,056)
Distributions declared	-	-	(9,829,851)	-	(9,829,851)
Equity, December 31, 2008	<u>\$ 79,750,666</u>	<u>\$ (17,929,355)</u>	<u>\$ (37,496,464)</u>	<u>\$ 13,104,637</u>	<u>\$ 37,429,484</u>

Year Ended December 31, 2007:

	Units	Cumulative Loss	Cumulative Distributions	Equity Component of Debentures	Total
Equity, December 31, 2006	\$ 77,812,493	\$ (6,921,395)	\$ (17,898,958)	\$ 13,764,313	\$ 66,756,453
Conversion of debentures	250,659	-	-	(35,656)	215,003
Issue costs	(44,049)	-	-	-	(44,049)
Maturity of Series A debentures	301,362	-	-	(301,362)	-
Exercise of unit options	40,000	-	-	-	40,000
Unit-based compensation	309,233	-	-	-	309,233
Units issued on distribution reinvestment plan	454,909	-	-	-	454,909
Loss and comprehensive loss	-	(1,400,904)	-	-	(1,400,904)
Distributions declared	-	-	(9,767,655)	-	(9,767,655)
Equity, December 31, 2007	<u>\$ 79,124,607</u>	<u>\$ (8,322,299)</u>	<u>\$ (27,666,613)</u>	<u>\$ 13,427,295</u>	<u>\$ 56,562,990</u>

The accompanying notes are an integral part of these financial statements.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS

	Year Ended December 31	
	2008	2007
Revenue		
Rentals from income properties (Note 18)	\$ 65,847,271	\$ 45,216,274
Interest and other income	<u>955,023</u>	<u>1,095,041</u>
	66,802,294	46,311,315
Expenses		
Property operating costs	<u>24,732,149</u>	<u>19,238,660</u>
Income before the undernoted	<u>42,070,145</u>	<u>27,072,655</u>
Financing expense (Note 19)	36,291,778	23,015,545
Trust expense	2,622,973	2,056,789
Amortization (Note 20)	<u>11,408,548</u>	<u>8,174,795</u>
	<u>50,323,299</u>	<u>33,247,129</u>
Loss before income taxes	(8,253,154)	(6,174,474)
Future income tax expense (recovery) (Note 11)	<u>1,266,042</u>	<u>(4,732,863)</u>
Loss before non-controlling interest	(9,519,196)	(1,441,611)
Non-controlling interest (Note 13)	<u>(87,860)</u>	<u>40,707</u>
Loss and comprehensive loss for the year	<u>\$ (9,607,056)</u>	<u>\$ (1,400,904)</u>
Loss per unit (Note 22)		
Basic	\$ (0.549)	\$ (0.080)
Diluted	\$ (0.549)	\$ (0.080)
Weighted average number of units (Note 22)		
Basic	17,485,603	17,457,299
Diluted	17,485,603	17,457,299

The accompanying notes are an integral part of these financial statements.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended December 31	
	2008	2007
Cash provided by (used in) operating activities		
Loss for the year	\$ (9,607,056)	\$ (1,400,904)
Items not affecting cash		
Straight-line rent adjustment	(10,903)	(58,618)
Accretion on debt component of convertible debentures	2,469,702	2,004,220
Unit-based compensation	391,517	309,233
Amortization (Note 20)	13,160,148	9,936,080
Change in fair value - swap asset	4,012,403	-
Future income taxes	1,266,042	(4,732,863)
Non-controlling interest	87,860	(40,707)
	11,769,713	6,016,441
Changes in non-cash operating items (net of effects of acquisition of income properties)	1,238,353	1,168,265
Tenant inducements and leasing expenditures incurred through leasing activity	(592,552)	(105,479)
	<u>12,415,514</u>	<u>7,079,227</u>
Cash provided by (used in) financing activities		
Proceeds of mortgage loan financing	132,885,288	180,042,264
Repayment of Series A debentures	-	(1,677,000)
Repayment of Series D debentures	(1,593,000)	-
Repayment of mortgage loans on refinancing	(38,066,146)	(31,232,909)
Repayment of principal on mortgage loans	(6,771,886)	(4,795,045)
Expenditures on transaction costs	(1,340,590)	(1,773,800)
Units purchased and cancelled under normal course issuer bid	(1,778,440)	-
Distributions paid on units (Note 21)	(8,104,253)	(9,336,147)
Distributions paid on LP units of Village West LP	(199,705)	(199,705)
	<u>75,031,268</u>	<u>131,027,658</u>
Cash provided by (used in) investing activities		
Acquisition of income properties	(46,865,000)	(91,191,965)
Payment of acquisition cost payable	(19,615,893)	-
Construction of income properties	(4,972,385)	(3,890,777)
Improvements to income properties	(3,565,986)	-
Increase in properties under development	(8,248,758)	(34,231,084)
Mortgage loan receivable advance	-	(10,000,000)
Deposits on potential acquisitions	(1,010,000)	(600,000)
Increase in restricted cash	(1,315,217)	(1,404,981)
	<u>(85,593,239)</u>	<u>(141,318,807)</u>
Cash increase (decrease)	1,853,543	(3,211,922)
Cash (bank indebtedness), beginning of year	(1,623,651)	1,588,271
Cash (bank indebtedness), end of year	\$ 229,892	\$ (1,623,651)
Supplementary cash flow information (Note 21)		

The accompanying notes are an integral part of these financial statements.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

1 *Organization*

Lanesborough Real Estate Investment Trust ("the Trust") is a closed-end real estate investment trust which was created under a Declaration of Trust dated April 23, 2002 and amended on June 12, 2006 and on June 18, 2008.

2 *Significant accounting policies*

The accompanying financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP"). These financial statements reflect the operations of the Trust and wholly owned operating subsidiaries and LREIT Village West Limited Partnership ("Village West LP"), an entity controlled by the Trust. All inter-entity transactions have been eliminated.

Change in accounting policy

On January 1, 2008, the Trust adopted CICA Handbook Section 1535 - Capital Disclosures, Section 3862 - Financial Instruments - Disclosures and Section 3863 - Financial Instruments - Presentation. Section 1535 requires the Trust to disclose information that enables users of its financial statements to evaluate the Trust's objectives, policies and processes for managing capital. Sections 3862 and 3863 replace the existing Section 3861, Financial Instruments - Disclosure and Presentation. These new sections revise and enhance disclosure requirements and carry forward unchanged existing presentation requirements. These new sections require disclosures about the nature and extent of risks arising from financial instruments and how the Trust manages those risks. The new standards do not have any impact on the classification or measurement of financial instruments.

Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as at the date of the financial statements and the reported amounts of revenue and expenses during the year. Actual results could differ from those estimates and as adjustments become necessary, the adjustments are reported in earnings in the year in which the adjustments become known.

Significant items subject to estimates include the allocation of the total cost to income properties on acquisition, the transfer of amounts from properties under development to income properties, the remaining useful life of the income properties, undiscounted cash flows to be generated from income properties, the calculation of future income tax assets and liabilities and the completion of the Parsons Landing acquisition.

Income properties

Income properties include land, buildings and related costs and improvements, furniture, equipment and appliances, tenant inducements and leasing expenses and intangible assets.

Income properties are carried at cost. Tenant inducements and leasing expenses that are incurred to obtain a lease are capitalized to the cost of buildings and improvements.

A portion of the total cost of acquisition of an income property is allocated to reflect the tenant origination costs (tenant inducements and leasing expenses) associated with in-place leases. A portion of the total cost of acquisition of an income property is also allocated to intangible assets to reflect the cost of lease origination costs, tenant relationships and above market leases.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007****2 *Significant accounting policies (continued)******Income properties (continued)***

If events or circumstances indicate that the carrying value of the income properties may be impaired, a recoverability analysis is performed based upon estimated undiscounted cash flows to be generated from the income properties. If the analysis indicated that the carrying value is not recoverable from future cash flows, the income properties are written down to estimated fair value and an impairment loss is recognized.

Amortization on buildings is recorded on a straight-line basis over their remaining useful lives ranging from 25 to 50 years. Amortization of improvements is recorded on a straight-line basis over their remaining useful lives ranging from 5 to 25 years. Amortization of tenant inducements and leasing expenses is recorded on a straight-line basis over the term of the respective leases. Amortization of furniture, equipment and appliances is recorded on a straight-line basis over their remaining useful lives ranging from 5 to 15 years. Amortization of intangible assets is recorded on straight-line basis over the term of respective leases.

Carrying costs during major renovations

Carrying costs incurred in regard to major in-suite renovations of income properties are capitalized in the cost of the building. Major in-suite renovations involve the temporary removal of suites from the rental market and include the replacement of flooring, draperies, appliances and cabinetry as well as related repairs and painting. Carrying costs consist of financing and certain property operating costs including property taxes, utilities, common area maintenance and salary costs relating to the suites removed from the rental market. The carrying costs are amortized at such a time as the suites are returned to the rental market with an estimated useful life of five years.

Properties under development

Properties under development are stated at cost. Cost is comprised of acquisition costs, external and internal development and initial leasing costs, property operating costs and financing expenses less rental revenue incurred during the period of development prior to achieving a satisfactory level of occupancy within a predetermined time period.

Mortgage loans receivable

Mortgage loans receivable are stated at amortized cost. If events or circumstances indicate that the carrying value of a mortgage loan receivable may be impaired, the mortgage loan receivable is classified as impaired and reduced to its estimated fair value.

Intangible liabilities

A portion of the total cost of acquisition of an income property is allocated to intangible liabilities to reflect the cost of below market leases. If the carrying value is not realizable in the future, the intangible liabilities are adjusted to estimated fair value and a gain is recognized.

Convertible debentures

Convertible debentures are separated into debt and equity components based on the respective fair values at the date of issue. The fair value of the debt component of convertible debentures is estimated based on the present value of future interest and principal payments due under the terms of the debentures. The value assigned to the equity component represents the estimated fair value ascribed to the holders' options to convert the debentures into units.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2008 AND 2007

2 *Significant accounting policies (continued)*

Derivative financial instruments

Derivative financial instruments are utilized to reduce interest rate risk on the mortgage loans payable. The Trust does not enter into financial instruments for trading or speculative purposes.

Interest rate swap agreements are used as part of the Trust's program to manage the fixed and floating interest rate mix of the Trust's total mortgage loan portfolio and related overall cost of borrowing. The interest rate swap agreements involve the periodic exchange of payments without the exchange of the notional principal amount upon which the payments are based. The interest rate swap agreements are classified as held-for-trading and are recorded on the balance sheet at fair value. The change in fair value is recognized as an adjustment to financing expense. The related amount payable to or receivable from counterparties is included as an adjustment to accrued interest.

Unit options

The Trust has a unit option plan available for trustees, officers and employees of the Trust, as well as management company employees of the Trust, including Shelter Canadian Properties Limited and consultants retained by the Trust including investor relations consultants. Consideration paid by option holders on exercise of unit options is credited to Equity. The fair value based method of accounting is applied to all unit-based compensation. The fair value of the unit options granted is estimated on the date of grant using the Black-Scholes option pricing model. Compensation expense in regard to options granted to officers, employees and trustees is recognized over the vesting period of the options. Compensation expense in regard to options issued to Shelter Canadian Properties Limited under the services agreement is recognized over the initial term of the services agreement.

Revenue recognition

Rents are recognized as revenue over the terms of the related lease agreements. Rental revenue from leases with contractual rent increases is recognized on a straight-line basis over the term of the respective leases. The difference between the rental revenue recognized and the amount contractually due under the lease agreements is recorded to straight-line rent receivable and accrued rental revenue. Recoveries from tenants for property operating costs and property taxes are recognized as revenue during the year in which the applicable costs are incurred. Meal and other revenue is recognized as earned.

Income taxes

In accordance with the terms of the Declaration of the Trust, the Trust intends to distribute its income for income tax purposes each year to such an extent that it will not be liable for income taxes under Part 1 of the Income Tax Act.

In June 2007, new legislation relating to, among other things, the federal income taxation of publicly traded income trusts was enacted. Under the new rules, certain distributions from a "specified investment flow-through" trust (a "SIFT") will no longer be deductible in computing a SIFT's taxable income, and a SIFT will be subject to tax on such distributions at a rate that is substantially equivalent to the general tax rate applicable to a Canadian corporation. Distributions paid as returns of capital will not be subjected to this tax.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**2 *Significant accounting policies (continued)******Income Taxes (continued)***

The new rules do not apply to a "real estate investment trust" that meets prescribed conditions relating to the nature of its income and investments (a "Qualifying REIT"). In the opinion of management, the Trust does not currently satisfy the prescribed conditions. The new legislation is not expected to apply to the Trust until 2011 as it provides for a transition period for publicly traded entities that existed prior to November 1, 2006. Prior to 2011, the Trust will consider its alternatives, including restructuring its affairs in order to meet the prescribed conditions and become a Qualifying REIT.

As the Trust does not currently meet the criteria for a Qualifying REIT, GAAP requires that the future income tax asset and liability calculation and estimates reflect its current income tax status, notwithstanding the intent of the Trust to become a Qualifying REIT prior to 2011 to the extent possible.

In accordance with GAAP, the Trust is required to: (i) determine its temporary differences between asset balances for income tax purposes and the balances recorded in accordance with GAAP; (ii) determine the periods over which those temporary differences are expected to reverse; and (iii) apply the tax rates enacted at the balance sheet date that will apply in the periods those temporary differences are expected to reverse. The Trust is required to use reasonable estimates in completing the calculation and the result of the calculation is recorded as a future income tax asset or liability.

Wholly-owned operating subsidiaries of the Trust are operating businesses and provide for income tax expense using the asset and liability method of accounting for income taxes at enacted or substantively enacted rates. Current income taxes are recognized for the estimated income taxes payable for the current year. Future income tax assets and liabilities are recognized for temporary differences between tax and accounting bases of assets and liabilities, as well as the benefit of losses available to be carried forward to future years for tax purposes that are more likely than not to be realized.

Comprehensive income

The Trust does not have any other comprehensive income or accumulated other comprehensive income.

Per unit calculations

Basic per unit amounts are calculated using the weighted average number of units outstanding during the year, including vested deferred units. Diluted per unit amounts are calculated after considering the potential exercise of convertible debentures, exchangeable Class B Limited Partnership units of Village West LP, unvested deferred units, and outstanding unit options. The dilutive effect on per unit amounts resulting from outstanding unit options is calculated using the treasury stock method. Under this method, the diluted weighted average number of units is calculated assuming the proceeds that arise from the exercise of the outstanding options are used to purchase units of the Trust at their average market price for the period.

Financial instruments

All financial instruments are measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held for trading, available for sale, held to maturity, loans and receivables, or other liabilities.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 20072 **Significant accounting policies (continued)****Financial instruments (continued)**

Financial assets and financial liabilities classified as held-for-trading are measured at fair value with gains and losses recognized in net earnings. Financial assets classified as held-to-maturity, loans and receivables and other financial liabilities (other than those held-for-trading) are measured at amortized cost using the effective interest rate method of amortization. Available-for-sale financial assets are measured at fair value with unrealized gains and losses recognized in other comprehensive income. Investments in equity instruments classified as available-for-sale that do not have a quoted market price in an active market are measured at cost.

Net gains and losses arising from changes in fair value of loans and receivables, held-to-maturity investments, and other liabilities are recognized in net income upon derecognition or impairment.

Derivative instruments are recorded on the balance sheet at fair value including those derivatives that are embedded in a financial instrument or other contract but are not closely related to the host financial instrument or contract, respectively. Changes in the fair values of derivative instruments are recognized in net earnings, except for derivatives that are designated as cash flow hedges, in which case the fair value change for the effective portion of such hedging relationships are recognized in other comprehensive income.

The Trust has designated its financial instruments, as follows:

<u>Financial Statement Item</u>	<u>Classification</u>	<u>Measurement</u>
Cash	Held for trading	Fair value
Mortgage loans receivable	Loans and receivables	Amortized cost
Other assets		
Amounts receivable	Loans and receivables	Amortized cost
Restricted cash	Held for trading	Fair value
Mortgage loans payable	Other financial liabilities	Amortized cost
Accounts payable and accrued liabilities		
Interest rate swap	Held for trading	Fair value
Other accounts payable and accrued liabilities	Other financial liabilities	Amortized cost
Convertible debentures - debt component	Other financial liabilities	Amortized cost
Bank indebtedness	Held for trading	Fair value

Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability. Transaction costs include fees and commissions paid to agents, advisers, brokers and dealers, levies by regulatory agencies and securities exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs. Transaction costs are expensed as incurred for financial instruments classified or designated as held for trading. For other financial instruments, transaction costs are capitalized in the cost of the related asset or liability on initial recognition and are measured at amortized cost using the effective interest rate method.

The Trust assesses impairment of all financial assets, except those classified as held for trading. Management considers whether there has been a breach in contract, such as default of interest or principal payments in determining whether objective evidence of impairment exists. Impairment is measured as the difference between the asset's carrying value and its fair value. Impairment is included in current earnings.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**2 Significant accounting policies (continued)****Future changes to significant accounting policies****(a) Goodwill and intangible assets**

In February 2008, the CICA issued a new Handbook Section 3064, "Goodwill and Intangible Assets". This new section replaces Section 3062, "Goodwill and Intangible Assets", and establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. Handbook Section 1000, Financial Statement Concepts, was also amended to provide consistency with this new standard. The new and amended standards will be effective for the Trust's 2009 fiscal year, and will be adopted on a retroactive basis with restatement of the prior years.

The new policy will not have any impact on the consolidated financial statements.

(b) International Financial Reporting Standards ("IFRS")

The CICA Accounting Standards Board has adopted a strategic plan for the direction of accounting standards in Canada. As part of the plan, accounting standards for public companies will be required to converge with International Financial Reporting Standards for fiscal years beginning on or after January 1, 2011 with comparative figures presented on the same basis. The International Financial Reporting Standards will replace Canada's current GAAP for public companies.

Management is currently in the process of evaluating the potential impact of the International Financial Reporting Standards to the consolidated financial statements. This will be an ongoing process as new standards and recommendations are issued by the International Accounting Standards Board and the CICA. The consolidated financial performance and financial position as disclosed in our current GAAP financial statements may be significantly different when presented in accordance with International Financial Reporting Standards.

The CICA has provided public companies with the option to early adopt International Financial Reporting Standards effective January 1, 2009. The Trust does not intend to adopt these standards on January 1, 2009.

(c) Business Combinations

CICA Handbook Section 1582 - Business Combinations will apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. CICA Handbook Sections 1601 - Consolidations and 1602 - Non-Controlling Interests will be effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Earlier adoption of these sections is permitted as of the beginning of a fiscal year. All three sections must be adopted concurrently. These sections replace the former CICA Handbook Sections 1581 - Business Combinations and 1600 - Consolidated Financial Statements. CICA Handbook Section 1601 establishes standards for the preparation of consolidated financial statements. CICA Handbook Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**3 Acquisitions**

During the year ended December 31, 2008, the Trust acquired three income properties.

The net assets acquired in the transaction are as follows:

Income properties	
Land	\$ 9,161,705
Buildings	114,167,293
Furniture, equipment and appliances	1,259,300
Asphalt and paving	5,892,900
Intangible assets	798,600
Mortgage loans payable assumed	(20,539,500)
Vendor take-back mortgage loan payable	<u>(4,000,000)</u>
	<u>\$106,740,298</u>
<u>Consideration:</u>	
Cash	\$ 46,865,000
Deposits paid in the year	1,450,000
Deposits paid in prior year	139,300
Mortgage loan receivable, applied to purchase	10,000,000
Acquisition cost payable	45,733,000
GST payable	<u>2,552,998</u>
	<u>\$106,740,298</u>

Parsons Landing

On September 1, 2008, the Trust acquired possession of Parsons Landing for a total consideration of \$63,200,000 including GST. Title to the income property will pass to the Trust upon payment of the balance of the acquisition cost payable.

The balance owing of the acquisition cost payable was due on February 28, 2009, with interest of \$1,077,594 from January 1, 2009 to February 28, 2009.

The mortgage financing for Parsons Landing has been delayed and, as a result, the vendor has agreed to extend the deadline for payment of the balance owing until May 29, 2009 with interest from March 1, 2009 of \$2,621,175. The vendor has also agreed to accept partial payment on account of interest of \$600,000, payable in two installments of \$300,000 in March and April of 2009 and to reduce the balance by \$1.4 Million on payment at closing. The payment extension is conditional upon the Trust obtaining a commitment for mortgage financing of \$45,000,000 by April 15, 2009. In the event that a financing commitment is not received by April 15, 2009 or any other act of default, the vendor shall be permitted to list the property for sale.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**4** *Income properties*

<u>December 31, 2008</u>	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
Land	\$ 88,689,716	\$ -	\$ 88,689,716
Buildings and improvements	476,182,353	(22,480,820)	453,701,533
Furniture, equipment and appliances	13,073,030	(2,787,885)	10,285,145
Intangible assets	<u>4,264,427</u>	<u>(2,850,535)</u>	<u>1,413,892</u>
	<u>\$582,209,526</u>	<u>\$ (28,119,240)</u>	<u>\$554,090,286</u>
 <u>December 31, 2007</u>	 <u>Cost</u>	 <u>Accumulated Amortization</u>	 <u>Net Book Value</u>
Land	\$ 70,228,011	\$ -	\$ 70,228,011
Buildings and improvements	311,293,608	(13,338,109)	297,955,499
Furniture, equipment and appliances	7,825,239	(1,557,893)	6,267,346
Intangible assets	<u>3,465,827</u>	<u>(2,120,384)</u>	<u>1,345,443</u>
	<u>\$392,812,685</u>	<u>\$ (17,016,386)</u>	<u>\$375,796,299</u>

The tenant at Lakewood Manor has the option to purchase the townhouse portion of the property for \$26,873,600 to June 30, 2009 and \$27,667,200 to June 30, 2010. The net book value of the townhouse portion of Lakewood Manor at December 31, 2008 is \$25,301,565.

At December 31, 2008, the carrying value of the income properties was not impaired.

5 *Properties under development*

	<u>December 31 2008</u>	<u>December 31 2007</u>
Clarington Seniors Residence	\$ 26,164,803	\$ 25,023,068
Elgin Lodge	9,792,971	9,766,638
Laird's Landing	<u>-</u>	<u>45,439,063</u>
	<u>\$ 35,957,774</u>	<u>\$ 80,228,769</u>

The cost of properties under development includes carrying costs of \$1,052,216 for the year ended December 31, 2008 (2007 - \$2,111,781).

6 *Mortgage loan receivable*

The mortgage loan receivable at December 31, 2007 consisted of a \$10,000,000, 8% second mortgage loan secured by Parsons Landing, a 163 suite multi-family apartment project in Fort McMurray, Alberta.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007

7 Other assets

	December 31 2008	December 31 2007
Amounts receivable	\$ 1,442,421	\$ 958,397
Prepaid expenses, deposits and other	2,317,519	1,606,986
Deposits on potential acquisitions	210,000	650,000
Straight-line rent receivable	302,451	291,548
Restricted cash	4,156,856	2,841,639
Above market in place leases, net of accumulated amortization of \$72,026, (2007 - \$61,855)	51,700	61,871
	<u>\$ 8,480,947</u>	<u>\$ 6,410,441</u>

Amounts receivable includes rent receivable of \$1,027,396 (2007 - \$547,827) net of an allowance for doubtful accounts of \$108,816 (2007 - \$91,557).

Restricted cash consists primarily of funds held in trust for residential tenant security deposits, as well as interest and repair reserves required by mortgage lenders of \$846,659 (2007 - \$641,028).

8 Mortgage loans payable

	Interest Rates at December 31, 2008		Weighted Average Term to Maturity	December 31 2008
	Range	Weighted Average Interest Rate		
Income properties				
Fixed rate mortgages	4.5% - 12.0%	6.4%	4.7 years	\$351,886,563
Floating rate mortgages	5.8% - 6.3%	5.8%	Demand	<u>80,500,000</u>
				<u>432,386,563</u>
Properties under development				
Fixed rate mortgages	5.8% - 16.0%	9.4%	0.7 year	11,370,000
Floating rate mortgages	5.8% - 6.8%	6.0%	Demand	<u>12,435,570</u>
				<u>23,805,570</u>
				456,192,133
Difference between contractual and market interest rates on mortgage loans assumed				110,798
Unamortized transaction costs				<u>(2,375,770)</u>
				<u>\$453,927,161</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**8 Mortgage loans payable (continued)**

The Trust has entered into interest rate swap arrangements whereby the interest rate on the floating rate mortgages in the amounts of \$20,763,272 and \$22,576,256 have been fixed at 5.74% and 5.82% for the five and ten year terms of the respective mortgages.

	Interest Rates at December 31, 2007		Weighted Average Term to Maturity	December 31 2007
	Range	Weighted Average Interest Rate		
Income properties				
Fixed rate mortgages	4.1% - 11.0%	5.9%	5.3 years	\$263,514,757
Floating rate mortgages	6.3% - 7.3%	7.1%	Demand	25,500,000
Non interest bearing vendor take-back second mortgage			Demand	<u>236,475</u>
				<u>289,251,232</u>
Properties under development				
Fixed rate mortgages	5.8% - 16.0%	9.4%	1.2 years	11,370,000
Floating rate mortgages	7.0% - 8.0%	7.0%	Demand	<u>42,647,928</u>
				<u>54,017,928</u>
				343,269,160
Difference between contractual and market interest rates on mortgage loans assumed				301,060
Unamortized transaction costs				<u>(2,236,177)</u>
				<u>\$341,334,043</u>

Approximate principal repayments are as follows:

Year ending December 31	
2009	\$164,656,923
2010	43,594,683
2011	13,886,333
2012	37,618,302
2013	24,963,804
Thereafter	<u>171,472,088</u>
	<u>\$456,192,133</u>

The difference between contractual and market interest rates on mortgage loans assumed is amortized over the term of the respective mortgages. The balance of \$110,798 (2007 - \$301,060) is net of accumulated amortization of \$747,875 at December 31, 2008 (2007 - \$557,613). The difference relates to mortgage loans assumed on acquisition of properties under development. The amortization of \$190,262 (2007 - \$557,613) for the year ended December 31, 2008 is recorded as a reduction of the carrying value of properties under development.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**8 Mortgage loans payable (continued)**

Certain of the mortgage loans payable are subject to covenants, including minimum debt service ratios. The Trust is in compliance with all covenants in regard to mortgage loans payable as at December 31, 2008.

Mortgage loans are secured by mortgage charges registered against the title of specific income properties and are secured by assignment of book debts, by assignments of rents and repayment guarantees.

9 Convertible debentures

The face value of the outstanding convertible debentures is as follows:

	December 31 2008	December 31 2007
Series D	\$ -	\$ 1,593,000
Series E	11,950,000	11,950,000
Series F	13,680,000	13,680,000
Series G	25,732,000	25,732,000
	<u>\$ 51,362,000</u>	<u>\$ 52,955,000</u>

The Series D debentures, which bore interest at 8%, matured on March 16, 2008. The Trust repaid \$1,593,000 in respect of the Series D debentures.

The Series E debentures bear interest at 8% and mature on February 17, 2010. The Series E debentures are convertible at the request of the holder at any time during the year ending February 17, 2009 at a conversion price per unit of \$7.15, and during the year ending February 17, 2010 at \$7.90.

The Series F debentures bear interest at 7.5%, mature on March 11, 2011 and are subordinate to the Series E debentures. The Series F debentures are convertible at the request of the holder at any time during the year ending March 11, 2009 at a conversion price per unit of \$6.00, during the year ending March 11, 2010 at \$6.60, and during the year ending March 11, 2011 at \$7.30.

The unsecured Series G debentures bear interest at 7.5%, mature on December 31, 2011 and are subordinate to the Series E debentures, and Series F debentures. The Series G debentures are convertible at the request of the holder at any time prior to their maturity date at a conversion price of \$7.00. The Trust has the right to redeem in whole or in part, the Series G debentures at par plus accrued interest, provided that the weighted average trading price of the units during the twenty consecutive trading days ending five trading days preceding the date on which the notice of redemption is given must not be less than 125% of the applicable conversion price for the period from December 31, 2009 to December 31, 2010 and at par plus accrued interest from December 31, 2010. Upon receipt of the notice of intent to redeem, the holders may elect to convert to units at the then applicable conversion price.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**9** *Convertible debentures (continued)*

During the year ended December 31, 2008 there were not any conversions of convertible debentures. During the year ended December 31, 2007, the holders of convertible debentures exercised their right to convert to units, as follows:

<u>Convertible Debentures</u>	<u>Conversion Price</u>	<u>Units Issued</u>		
Series A	\$ 6.00	2,166		
Series D	5.00	31,200		
Series E	6.50	7,692		

<u>December 31, 2008</u>	<u>Debt</u>	<u>Equity</u>	<u>Total</u>
Convertible debentures			
Series E - 8%, due February 17, 2010	\$ 11,081,742	\$ 2,835,690	\$ 13,917,432
Series F - 7.5%, due March 11, 2011	11,791,848	3,564,376	15,356,224
Series G - 7.5%, due December 31, 2011	<u>21,216,807</u>	<u>6,704,571</u>	<u>27,921,378</u>
	44,090,397	13,104,637	57,195,034
Unamortized transaction costs	<u>(1,662,431)</u>	<u>-</u>	<u>(1,662,431)</u>
	<u>\$ 42,427,966</u>	<u>\$ 13,104,637</u>	<u>\$ 55,532,603</u>

<u>December 31, 2007</u>	<u>Debt</u>	<u>Equity</u>	<u>Total</u>
Convertible debentures			
Series D - 8%, due March 16, 2008	\$ 1,565,705	\$ 322,658	\$ 1,888,363
Series E - 8%, due February 17, 2010	10,456,183	2,835,690	13,291,873
Series F - 7.5%, due March 11, 2011	11,113,418	3,564,376	14,677,794
Series G - 7.5%, due December 31, 2011	<u>20,072,606</u>	<u>6,704,571</u>	<u>26,777,177</u>
	43,207,912	13,427,295	56,635,207
Unamortized transaction costs	<u>(2,171,659)</u>	<u>-</u>	<u>(2,171,659)</u>
	<u>\$ 41,036,253</u>	<u>\$ 13,427,295</u>	<u>\$ 54,463,548</u>

The Series E and F convertible debentures of the Trust are secured by a security interest on all the property and assets of the Trust. The security interest ranks senior to the trust units and subordinate to mortgage loans payable and related collateral security.

The allocation of the convertible debentures to debt and equity components is based on the net present value of future interest and principal payments with an estimated cost of borrowing without conversion option of 15% for Series E, Series F and Series G debentures.

The accretion of the debt component for year ended December 31, 2008 of \$2,469,702 (2007 - \$2,004,220), which increases the debt component from the initial carrying amount, is included in financing expense.

The series E and F debentures provide for the outstanding amount of the debentures to become payable on demand upon default, under certain terms and conditions, of a mortgage loan or a convertible debenture. The Trust is in compliance with all covenants in regard to mortgage loans and convertible debentures as at December 31, 2008.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 200710 *Accounts payable and accrued liabilities*

	December 31 2008	December 31 2007
Accounts payable and accrued liabilities	\$ 4,298,537	\$ 2,191,916
Payable on acquisition of Parsons Landing	48,220,000	-
Payable on acquisition of Millennium Village	-	19,615,893
Construction costs payable	254,432	4,710,619
Mortgage and debenture interest payable	2,830,930	2,276,599
Tenant security deposits	3,695,263	2,535,202
Interest rate swap	4,012,403	-
Below market in-place leases, net of accumulated amortization of \$74,895 (2007 - \$66,498)	699	9,096
	<u>\$ 63,312,264</u>	<u>\$ 31,339,325</u>

The amount payable on the acquisition of Parsons Landing includes the acquisition cost payable in the amount of \$45,733,000 and is expected to be paid during the second quarter of 2009. The amount payable on the acquisition of Millennium Village was paid during 2008.

Included in accounts payable and accrued liabilities are \$31,420 (2007 - nil) of current income taxes payable relating to taxes payable by a wholly owned operating subsidiary.

Interest Rate Swap

The Trust entered into interest rate swap arrangements whereby the interest rate on the floating rate mortgages have been fixed for the five and ten year terms of the mortgages. The interest rate swap is a derivative financial instrument classified as held-for-trading and is recorded on the balance sheet at fair value. The change in the fair value is recognized in net income.

Included in financing expense is a charge of \$4,012,403 for the year ended December 31, 2008.

11 *Future income taxes*

Future income taxes consists of the following components:

	December 31 2008	December 31 2007
Future income tax asset relating to the assets of Trust:		
Future income tax asset relating to the temporary difference between the accounting and tax basis held in the Trust expected to reverse after 2010 for:		
Income properties	\$ 3,518,985	\$ 3,917,283
Transaction costs	(89,554)	(153,522)
	<u>\$ 3,429,431</u>	<u>\$ 3,763,761</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 200711 *Future income taxes (continued)*

	Year ended December 31	
	2008	2007
Future income tax liability relating to the wholly owned subsidiaries:		
Future income tax liability relating to the temporary differences between the accounting and tax basis of income properties held in wholly owned subsidiaries	\$ 3,518,197	\$ 3,507,101
Future income tax asset relating to operating losses of wholly owned subsidiaries	<u>(1,569,604)</u>	<u>(889,196)</u>
	1,948,593	2,617,905
Valuation allowance	<u>1,569,604</u>	<u>-</u>
	<u>\$ 3,518,197</u>	<u>\$ 2,617,905</u>
Future income tax expense (recovery):		
Decrease (increase) in future income tax asset resulting from a change in temporary differences relating to:		
Income properties	\$ 211,762	\$ (3,917,283)
Transaction costs	(56,658)	153,522
Decrease (increase) in future income tax asset resulting from a change in tax rate for:		
Income properties	186,537	-
Transaction costs	<u>(7,311)</u>	<u>-</u>
	<u>334,330</u>	<u>(3,763,761)</u>
Wholly owned subsidiaries		
Increase in future income tax liability resulting from a change in temporary differences relating to income properties	73,769	216,742
Decrease in future income tax liability resulting from changes in tax rates	(62,673)	(409,208)
Increase in future income tax asset resulting from operating losses	(705,116)	(788,759)
Decrease in future income tax asset resulting from changes in tax rates	24,708	12,123
Valuation allowance	<u>1,569,604</u>	<u>-</u>
	900,292	(969,102)
Current income taxes at statutory tax rates	<u>31,420</u>	<u>-</u>
	<u>931,712</u>	<u>(969,102)</u>
	<u>\$ 1,266,042</u>	<u>\$ (4,732,863)</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**11 Future income taxes (continued)**

The wholly owned subsidiaries have the following operating losses available to reduce income for tax purposes in future years. The potential benefit of these losses has not been reflected in the consolidated financial statements.

Operating losses carried forward expiring in:

2026	\$ 113,256
2027	2,349,986
2028	<u>2,437,741</u>
	<u>\$ 4,900,983</u>

12 Cash and bank indebtedness

Cash and (bank indebtedness) consists of cash in bank less a revolving line of credit. The Trust obtained a revolving chartered bank line of credit in 2007 in the maximum amount of \$5,000,000, bearing interest at prime and repayable on demand. The line of credit is secured by a second mortgage on an income property. The amount available on the line of credit is reduced by \$125,000 relating to the issue of a letter of credit. As at December 31, 2008, \$1,555,000 (2007 - \$1,960,000) is available to the Trust under the terms of the line of credit.

Cash and (bank indebtedness) consist of the following:

	December 31 2008	December 31 2007
Cash in bank	\$ 3,549,892	\$ 1,416,349
Less: Line of credit	<u>(3,320,000)</u>	<u>(3,040,000)</u>
	<u>\$ 229,892</u>	<u>\$ (1,623,651)</u>

13 Non-controlling interest

Non-controlling interest represents the interest of the holder of the Class B units (LP Units) of Village West LP, an entity controlled by the Trust, which is consolidated in the financial statements. The holder of the LP Units of Village West LP is entitled to receive distributions equal to those provided to holders of units of the Trust. LP Units are transferable and are exchangeable, at the option of the holder on a one for one basis for units of the Trust. As at December 31, 2008, there were 356,617 (2007 - 356,617) LP Units of Village West LP outstanding.

The change in non-controlling interest is summarized as follows:

	December 31 2008	December 31 2007
Balance, beginning of year	\$ 1,685,103	\$ 1,925,515
Share of income (loss) of Village West Townhouses	87,860	(40,707)
Distributions on LP Units of Village West LP	<u>(199,705)</u>	<u>(199,705)</u>
Balance, end of year	<u>\$ 1,573,258</u>	<u>\$ 1,685,103</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**14 Related party transactions**

Related party transactions have occurred in the normal course of operations and are measured at the exchange amount which is the amount established and agreed by the related parties. Shelter Canadian Properties Limited is a related party by virtue of the property management and services agreements with the Trust.

Management agreement

On August 7, 2007 the Trust renewed the property management agreement with Shelter Canadian Properties Limited with the same terms and conditions, for a five year term expiring on August 30, 2012. Under the property management agreement, Shelter Canadian Properties Limited will administer the day-to-day operations of the Trust's portfolio of income properties, except for the seniors housing complexes. The Trust pays property management fees equal to 4% of gross receipts from the income properties owned by the Trust. In regards to commercial properties, Shelter Canadian Properties Limited is also entitled to leasing commissions on new leases of 3% to 5% of base rental payments and leasing commissions on renewal of 1 1/2% to 2 1/2% of base rental payments. Shelter Canadian Properties Limited is also entitled to tenant improvement and renovation fees equal to 5% of the total cost of such work.

The Trust incurred property management fees payable to Shelter Canadian Properties Limited of \$2,456,258 for the year ended December 31, 2008 (2007 - \$1,605,530). Property management fees are included in property operating costs and during the period of major in-suite renovations or development are capitalized to the cost of buildings and properties under development.

The Trust incurred leasing commissions on commercial properties to Shelter Canadian Properties Limited of \$40,938 for the year ended December 31, 2008 (2007 - \$32,876). The amounts are capitalized to income properties.

Included in accounts payable and accrued liabilities at December 31, 2008 is a balance of \$125,691 (2007 - \$98,802), payable to Shelter Canadian Properties Limited in regard to outstanding property management fees.

Services agreement

The Trust entered into a services agreement, for an initial term expiring August 30, 2007, with Shelter Canadian Properties Limited. Under the services agreement, Shelter Canadian Properties Limited provides the Trust management and support services for the administration of the day-to-day activities of the Trust. Effective January 1, 2006, the services agreement was amended to provide for a service fee payable to Shelter Canadian Properties Limited, equal to 0.3% of the net book value of the assets of the Trust, excluding cash and accumulated amortization. The services agreement was renewed with the same terms and conditions until June 30, 2009.

The Trust incurred service fees payable to Shelter Canadian Properties Limited of \$1,661,308 for the year ended December 31, 2008 (2007 - \$1,176,967). Service fees are included in trust expense.

Included in accounts payable and accrued liabilities at December 31, 2008 is a balance of nil (2007 - \$265,902), payable to Shelter Canadian Properties Limited in regard to outstanding service fees.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**14 Related party transactions (continued)****Acquisition**

The Trust has entered into a development agreement with Shelter Canadian Properties Limited to develop Laird's Landing, a residential property located in Fort McMurray, Alberta. During the year ended December 31, 2008, the development and construction supervision services provided by Shelter Canadian Properties Limited were completed and \$234,179 (2007 - \$431,421) was recorded to properties under development.

Included in construction costs payable on properties under development is a balance of nil (2007 - \$553,826) payable to Shelter Canadian Properties Limited in regard to the development and construction services.

Guarantees

Certain of the mortgage loans payable have been guaranteed by Shelter Canadian Properties Limited. There were not any fees charged in regard to the guarantees.

15 Units

The number of units issued, and purchased and cancelled, are as follows:

	Year Ended December 31	
	2008	2007
Outstanding, beginning of year	17,529,894	17,392,235
Issued on conversion of debentures	-	41,058
Issued on distribution reinvestment plan	514,387	86,601
Issued on exercise of unit option	-	10,000
Purchased and cancelled under normal course issuer bid	(456,200)	-
Outstanding, end of year	<u>17,588,081</u>	<u>17,529,894</u>

Distribution Reinvestment Plan

Pursuant to the distribution reinvestment plan ("DRIP"), holders of Units may elect to have all or a portion of their regular monthly distributions automatically reinvested in additional Units. Participants in the DRIP receive a bonus distribution of units equal to 4% of the amount of the cash distribution which is reinvested. The purchase price of the units is equal to the weighted average closing price of the Units for the five trading days immediately preceding the distribution payment date. During the year ended December 31, 2008, 514,387 (2007 - 86,601) units have been issued pursuant to the DRIP.

Units purchased and cancelled under normal course issuer bid

On January 16, 2008, the Trust announced its intention to make a normal course issuer bid to acquire up to 876,494 units, representing 5% of the issued and outstanding units of the Trust, over the twelve month period ended January 20, 2009, in accordance with the policies of the Toronto Stock Exchange. Units purchased by the Trust under its normal course issuer bid are cancelled. During the year ended December 31, 2008 the Trust has purchased and cancelled 456,200 units under its normal course issuer bid at a weighted average price of \$3.90 per unit.

On January 21, 2009, the Trust announced its intention to make a normal course issuer bid to acquire up to 877,404 units, representing 5% of the issued and outstanding units of the Trust, over the twelve month period ending January 22, 2010.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007

16 Unit option plan

On January 7, 2008, the Trust granted options to each of the four independent trustees, the chief executive officer, the chief financial officer and to a total of 20 management and other senior employees of Shelter Canadian Properties Limited who are engaged in functions related to the Trust, to acquire an aggregate of 370,000 units, exercisable at \$5.10 per unit. The options granted to each of the four independent trustees vested immediately. The balance of the options granted will vest equally on each of the grant date and the first, second, third and fourth anniversaries of the grant date. The units issued upon exercise of the options will be subject to a minimum hold period of four months and a day from the date of the grant of the options.

The fair value of each unit option granted is estimated on the date of grant using the Black-Scholes option pricing model. The assumptions used for the options granted on January 7, 2008 are dividend yield of 10.32%, expected volatility of 35.59%, risk-free interest rate of 3.68% and life of options of five years. The total fair value of the unit options granted on January 7, 2008 is \$241,892.

Unit-based compensation expense of \$391,517 for the year ended December 31, 2008 (2007 - \$301,727), relating to options issued was recorded to expense the fair value unit-based compensation, including \$177,930 for the year ended December 31, 2008 relating to the options issued on January 7, 2008. Unit-based compensation is included in trust expense.

A summary of the status of the unit options and changes during the year is as follows:

	Year Ended December 31, 2008		Year Ended December 31, 2007	
	Units	Weighted Average Exercise Price	Units	Weighted Average Exercise Price
Outstanding, beginning of year	1,110,000	\$ 5.72	1,000,000	\$ 5.77
Granted, June 8, 2007	-	-	120,000	5.30
Exercised, October 26, 2007	-	-	(10,000)	4.00
Granted, January 7, 2008	370,000	5.10	-	-
Expired, August 11, 2008	(28,000)	5.73	-	-
Outstanding, end of year	<u>1,452,000</u>	<u>\$ 5.56</u>	<u>1,110,000</u>	<u>\$ 5.72</u>
Vested, end of year	<u>960,400</u>		<u>654,000</u>	

At December 31, 2008 the following unit options were outstanding:

Exercise price	Options outstanding	Options vested	Expiry date
\$ 5.42	30,000	30,000	January 17, 2011
5.80	935,000	641,000	July 26, 2011
5.30	120,000	120,000	June 8, 2012
5.10	<u>367,000</u>	<u>169,400</u>	January 7, 2013
	<u>1,452,000</u>	<u>960,400</u>	

LANESBOROUGH REAL ESTATE INVESTMENT TRUST**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007****17 *Deferred unit plan***

On June 18, 2008, the Trust adopted a deferred unit plan, under which, any trustee, officer, employee, or consultant employee of the Trust may elect to have their annual bonus, annual board retainer or board meeting fees payable to that person by the Trust paid in the form of deferred units. The number of deferred units received by a participant is determined by dividing the amount of the annual bonus, annual board retainer or board meeting fees as applicable to be paid in the form of deferred units on that date by the fair market value of the Trust's units.

Deferred units granted to Trustees shall vest immediately. Deferred units granted to participants other than Trustees shall vest 33% on the first anniversary of grant, 33% on the second anniversary of grant, and 34% on the third anniversary of grant. In the event of any change of control, any unvested deferred units shall vest upon the earlier of the next applicable vesting date and the date that is immediately prior to the date upon which the change of control is completed. The board shall have the discretion to vary the manner in which deferred units vest for any participant.

The deferred units credited to a participant (including deferred units that have not yet vested) shall vest immediately and be redeemable by the participant following the termination other than for cause, retirement, or death, of the participant. In the event that a participant is terminated for cause, only the deferred units that have vested shall be redeemable and any unvested deferred units shall be cancelled.

Whenever cash distributions are paid on the units of the Trust, additional deferred units will be credited to the participant based on the number of deferred units held, the amount of the distribution and the market value of a unit of the Trust on the date of the distribution. Additional deferred units shall vest at the same time and on the same basis as the deferred units in respect of which they are credited.

Deferred units granted to Trustees totaled 23,528 for the year ended December 31, 2008 and 23,528 aggregate deferred units were outstanding at December 31, 2008.

Unit-based compensation expense of \$78,787 for the year ended December 31, 2008, relating to deferred units granted was recorded to expense the fair value unit-based compensation. Unit-based compensation is included in trust expense.

18 *Rentals from income properties*

Rental revenue contractually due from tenants includes the recovery of property operating costs and property taxes from tenants of \$2,918,646 (2007 - \$2,244,485) for the year ended December 31, 2008.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**19** *Financing expense*

	Year Ended December 31	
	2008	2007
Mortgage loan interest	\$ 24,116,087	\$ 15,092,084
Convertible debenture interest	3,943,760	4,159,555
Accretion of the debt component of convertible debentures	2,469,702	2,004,220
Amortization of transaction costs	1,749,826	1,759,686
Change in fair value of interest rate swap	4,012,403	-
	<u>\$ 36,291,778</u>	<u>\$ 23,015,545</u>

20 *Amortization*

	Year Ended December 31	
	2008	2007
Building	\$ 9,448,404	\$ 6,551,383
Furniture, equipment and appliances	1,229,992	637,624
Intangible assets, except for in-place leases	<u>730,152</u>	<u>985,788</u>
	11,408,548	8,174,795
Transaction costs	1,749,826	1,759,686
Above market in-place leases	10,171	10,357
Below market in-place leases	<u>(8,397)</u>	<u>(8,758)</u>
	13,160,148	9,936,080
Difference between contractual and market interest rates on mortgage loans assumed on properties under development	<u>(190,262)</u>	<u>(557,613)</u>
	<u>\$ 12,969,886</u>	<u>\$ 9,378,467</u>

21 *Supplementary cash flow information*

	Year Ended December 31	
	2008	2007
Interest paid and received		
Interest paid on mortgage loans	<u>\$ 23,565,791</u>	<u>\$ 14,215,038</u>
Interest paid on convertible debentures	<u>\$ 3,982,686</u>	<u>\$ 4,484,041</u>
Interest received on mortgage loans receivable	<u>\$ 313,865</u>	<u>\$ 717,356</u>
Other interest received	<u>\$ 669,583</u>	<u>\$ 470,430</u>
Cash distributions		
Distributions declared	\$ 9,829,851	\$ 9,767,655
Distributions to participants in the DRIP	<u>(1,725,598)</u>	<u>(431,508)</u>
Distributions paid on units	<u>\$ 8,104,253</u>	<u>\$ 9,336,147</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**22 Per unit calculations**

Basic per unit information is calculated based on the weighted average number of units outstanding for the year, including vested deferred units. Diluted per unit information is calculated based on the weighted average diluted number of units for the year, considering the dilutive effect of unvested deferred units, the potential exercise of outstanding unit options to the extent that the unit options are dilutive and the potential conversion of outstanding convertible debentures to the extent that the debentures are dilutive and the potential conversion of the outstanding Class B units of Village West LP to the extent that the units are dilutive.

Loss per unit calculations are based on the following:

	Year Ended December 31	
	2008	2007
Income (loss)	<u>\$ (9,607,056)</u>	<u>\$ (1,400,904)</u>
Diluted income (loss)	<u>\$ (9,607,056)</u>	<u>\$ (1,400,904)</u>
Units	17,483,454	17,457,299
Vested deferred units	<u>2,149</u>	<u>-</u>
Weighted average basic number of units	<u>17,485,603</u>	<u>17,457,299</u>
Weighted average diluted number of units	<u>17,485,603</u>	<u>17,457,299</u>

23 Distribution of income

In accordance with the Declaration of Trust, the Trust shall make cash distributions in an amount not less than the aggregate of taxable income from operations and realized capital gains, net of any realized allowable capital losses.

The minimum distribution required by the Declaration of Trust is nil (2007 - nil) for the year ended December 31, 2008.

24 Financial instruments and risk management**Risk management**

In the normal course of business, the Trust is exposed to financial risk that arises from its indebtedness, including fluctuations in interest rates and in the credit quality of its tenants. Management's involvement in operations helps identify risks and variations from expectations. As a part of the overall operation of the Trust, management takes steps to avoid undue concentrations of risk. The Trust manages the risks, as follows:

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**24 Financial instruments and risk management (continued)****Liquidity risk**

In addition to the liquidity risk relating to the mortgage financing for Parsons Landing, liquidity risk arises from the possibility of the Trust not having sufficient debt and equity capital available to fund its growth and refinance its debt as it matures.

The economic uncertainty which currently exists throughout the global marketplace has resulted in a more conservative and restrictive lending market.

The risk associated with the refinancing of maturing debt is mitigated as the maturity dates of the mortgage portfolio are staggered over a number of years and, except for properties under development, by limiting the use of floating interest rate debt.

As at December 31, 2008, the weighted average term to maturity of the fixed rate mortgages on income properties, excluding properties under development, is 4.7 years (2007 - 5.3 years).

The repayment obligations in regard to mortgage loans payable and convertible debentures are as follows:

Year ending December 31	Mortgage Loans Payable	Convertible Debentures	Total
2009	\$164,656,923	\$ -	\$164,656,923
2010	43,594,683	11,950,000	55,544,683
2011	13,886,333	39,412,000	53,298,333
2012	37,618,302	-	37,618,302
2013	24,963,804	-	24,963,804
Thereafter	171,472,088	-	171,472,088
	<u>\$456,192,133</u>	<u>\$ 51,362,000</u>	<u>\$507,554,133</u>

Interest rate risk

Interest risk arises from debt financing including the risk that the Trust will not be able to refinance the mortgages with terms as favourable as those of existing mortgages. The risk is minimized by having the majority of the mortgage loans on fixed term arrangements. In addition, the maturity dates of the mortgages are staggered over a number of years to reduce the exposure in any one year. At December 31, 2008 the percentage of fixed rate mortgage loans to total mortgage loans was 80% (2007 - 80%).

As at December 31, 2008, the Trust has total contractual mortgage principal maturities on income properties to December 31, 2011 of \$109,589,068, representing 24% of the mortgage loans principal balance. Should the amounts be refinanced upon maturity at an interest rate differential of 100 basis points, financing expense would increase by \$1,095,891 per year.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 200724 *Financial instruments and risk management (continued)***Interest rate risk (continued)**

The Trust has floating rate mortgages on income properties (excluding floating rate mortgages in the amount of \$20,763,272 and \$22,576,256, with interest rates fixed at 5.74 and 5.82 respectively by use of interest rate swap arrangements) totaling \$80,500,000.00, or 18.0% of the total mortgage loans principal balance as at December 31, 2008 (2007 - 8.8%).

Floating rate mortgages on properties under development comprise construction loans and loans on properties during the period of lease-up.

As at December 31, 2008, the Trust had total floating rate mortgages of \$92,935,570. Should interest rates increase by 100 basis points, financing expense would increase by \$929,356 per year.

With the exception of interest rate swap arrangements, the Trust does not trade in financial instruments.

Credit risk

Credit risk arises from the possibility that tenants may be unable to fulfil their lease commitments. The maximum exposure to credit risk is equal to the carrying value of the financial assets. The Trust has credit policies to address credit risk which include the analysis of financial position and credit history of a prospective tenant and by obtaining security deposits whenever permitted by legislation. An allowance for doubtful accounts or other impairment provisions are established based upon factors surrounding credit risk, historical trends and other information.

Thirteen properties, representing 51% of rentals from income properties, are located in Fort McMurray, Alberta. The credit risk associated with the tenants in Fort McMurray is mitigated due to the long-term nature of the oil sands industry and the credit worthiness of the commercial tenants which comprise a significant portion of the rent receivable. The Trust has a corporate tenant that accounts for 16% of rentals from income properties for the year ended December 31, 2008. Credit risk, in this regard, has been managed by the Trust leasing to a credit worthy tenant.

Rent is past due when a tenant has failed to make a payment when contractually due. The following is an aging of rent receivable past due but not impaired:

	December 31 2008	December 31 2007
<u>Rent receivable overdue:</u>		
0 to 30 days	\$ 372,485	\$ 24,567
31 to 60 days	123,340	85,866
More than 60 days	<u>271,116</u>	<u>171,904</u>
	<u>\$ 766,941</u>	<u>\$ 282,337</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**24 Financial instruments and risk management (continued)****Credit risk (continued)**

A reconciliation of allowance for doubtful accounts is as follows:

	December 31 2008	December 31 2007
Balance, beginning of year	\$ 42,185	\$ 55,256
Amount charged to bad debt expense relating to impairment of rent receivable	344,711	74,508
Amounts written off as uncollectible	<u>(278,080)</u>	<u>(87,579)</u>
Balance, end of year	<u>\$ 108,816</u>	<u>\$ 42,185</u>
Amount charged to bad debts as a percent of rentals from income properties	0.52%	0.16%

Currency risk

Currency risk is the risk that changes in foreign exchange rates may have an effect on future cash flows associated with financial instruments. The Trust does not have any transactions denominated in foreign currency and is not exposed to foreign currency risk.

Other price risk

Other price risk is the risk that changes in market prices, including commodity or equity prices, will have an effect on future cash flows associated with financial instruments. The cash flows associated with financial instruments of the Trust are not exposed to other price risk.

Fair values

Financial instruments include cash, mortgage loans receivable, amounts receivable, interest rate swap, restricted cash, mortgage loans payable, accounts payable and accrued liabilities, the debt component of convertible debentures, bank indebtedness and distributions payable. Except for the mortgage loans payable and the debt component of convertible debentures, the carrying values of these financial instruments approximate fair value due to the short term nature of the financial instruments.

The fair value of the mortgage loans payable are impacted by changes in market yields which can result in differences between the carrying value and fair value of the instruments. The fair value of mortgage loans payable has been estimated based on the current market rates for mortgages with similar terms and conditions. The estimated fair value of mortgage loans payable for the period ended December 31, 2008 is \$476,000,000 (December 31, 2007 - \$343,000,000).

The carrying value of the debt components of convertible debentures payable are impacted by changes in market yields which can result in differences between the carrying value and fair value of instruments. The fair value of the debt component of convertible debentures payable has been estimated based on the current market rates for debentures with similar terms and conditions. The estimated fair value of the debt component of convertible debentures payable for the period ended December 31, 2008 is \$33,290,680 (December 31, 2007 - \$43,207,912).

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 200725 *Management of capital*

The capital structure of the Trust is comprised of the following:

	December 31 2008	December 31 2007
Mortgage loans payable	<u>\$456,192,133</u>	<u>\$343,269,160</u>
Convertible debentures		
Debt component	44,090,397	43,207,912
Equity component	<u>13,104,637</u>	<u>13,427,295</u>
	<u>57,195,034</u>	<u>56,635,207</u>
Trust units	<u>79,750,666</u>	<u>79,124,607</u>
	<u>\$593,137,833</u>	<u>\$479,028,974</u>

The Trust manages capital in order to safeguard its ability to continue as a going concern; to ensure that returns are provided to Unitholders and to ensure an appropriate balance of risk and return.

The overall capital management strategy addresses the following considerations:

- The equity component of acquired properties is primarily funded from the proceeds of trust units or convertible debentures.
- Mortgage debt financing is arranged to optimize the leveraged returns from the real estate portfolio.
- Total mortgage debt financing is maintained within the overall debt limits as established by the Declaration of Trust. The Declaration of Trust provides for mortgage indebtedness of the Trust up to 75% of the appraised value of all properties.
- Whenever possible, the Trust will utilize fixed rate debt financing.
- Mortgage due dates are structured to reflect the properties being financed and debt maturity dates will be staggered, to the extent possible, in order to reduce refinancing risk.

The Trust monitors capital from time-to-time using a variety of measures. Monitoring procedures are performed as a part of the overall management of operations and are performed with the goal of enhancing the ability of the Trust to access capital and/or reduce the cost of capital.

In order to maintain or adjust the capital structure the Trust may issue units, debentures or mortgage debt; adjust the amount of distributions paid to unitholders; return capital to unitholders; purchase units; or reduce debt.

Market requirements for attracting capital may vary in ways that the Trust may not be able to accurately predict.

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 200726 *Segmented financial information*

The assets are located in and revenue is derived from the operation of commercial, light industrial and residential real estate in Canada. Commercial real estate consists of retail properties and office and retail mixed-use properties. Residential real estate consists of multi family residential properties and seniors housing complexes.

Year ended December 31, 2008:

	Commercial	Light Industrial	Residential	Trust	Total
Rentals from income properties	4,170,064	296,242	61,380,965	-	65,847,271
Interest and other income	34,508	1,371	469,375	449,769	955,023
Property operating costs	2,123,633	107,217	22,501,299	-	24,732,149
Financing expense	981,953	150,206	24,014,693	11,144,926	36,291,778
Amortization	898,021	31,345	10,479,182	-	11,408,548
Income (loss)	200,965	8,845	3,835,594	(13,652,460)	(9,607,056)
Total assets	26,727,508	2,761,923	571,755,474	943,425	602,188,330

Year ended December 31, 2007

	Commercial	Light Industrial	Residential	Trust	Total
Rentals from income properties	4,151,475	363,649	40,701,150	-	45,216,274
Interest and other income	27,834	1,217	331,812	734,178	1,095,041
Property operating costs	1,754,682	92,663	17,391,315	-	19,238,660
Financing expense	1,011,485	136,866	12,481,929	9,385,265	23,015,545
Amortization	860,383	31,345	7,283,067	-	8,174,795
Income (loss)	552,758	103,992	4,886,462	(6,944,116)	(1,400,904)
Total assets	18,742,321	2,729,861	442,275,294	12,451,794	476,199,270

Year ended December 31, 2008:

	Alberta	British Columbia	Manitoba	Ontario	Northwest Territories	Saskatchewan	Trust	Total
Rentals from income properties	38,059,684	1,468,901	7,030,747	1,598,621	6,004,036	11,685,282	-	65,847,271
Interest and other income	334,484	10,755	54,577	368	35,101	69,969	449,769	955,023
Property operating costs	10,619,589	875,505	3,330,600	1,028,862	2,459,794	6,417,799	-	24,732,149
Financing expense	18,688,558	338,398	1,897,763	728,342	1,287,642	2,206,149	11,144,926	36,291,778
Amortization	6,334,064	194,441	1,713,579	276,949	881,010	2,008,505	-	11,408,548
Income (loss)	2,751,955	71,313	143,383	(1,461,441)	1,410,692	1,129,502	(13,652,460)	(9,607,056)
Total assets	372,102,375	10,710,891	72,410,792	46,110,221	38,537,426	61,373,200	943,425	602,188,330

Year ended December 31, 2007

	Alberta	British Columbia	Manitoba	Ontario	Northwest Territories	Saskatchewan	Trust	Total
Rentals from income properties	20,548,300	1,439,007	5,792,407	1,872,594	5,051,458	10,512,508	-	45,216,274
Interest and other income	274,533	14,266	49,141	(61,194)	28,637	55,480	734,178	1,095,041
Property operating costs	6,367,049	872,869	2,628,237	1,218,702	2,057,851	6,093,952	-	19,238,660
Financing expense	7,674,083	353,961	1,575,248	648,191	1,210,037	2,168,760	9,385,265	23,015,545
Amortization	3,471,522	187,306	1,296,307	276,535	791,634	2,151,491	-	8,174,795
Income (loss)	3,310,182	39,138	341,753	263,624	1,020,573	567,942	(6,944,116)	(1,400,904)
Total assets	271,242,401	10,848,911	34,132,475	45,231,275	39,306,839	62,985,575	12,451,794	476,199,270

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 200727 *Commitments***Acquisitions****Parsons Landing Apartments**

On September 1, 2008, the Trust acquired possession of Parsons Landing, a residential property located in Fort McMurray, Alberta, for a total cost of \$63,200,000, including GST. On November 1, 2007, the Trust provided a \$10,000,000 second mortgage loan, which bore interest at 8%. On possession of Phase I of the property on May 14, 2008, a purchase installment payment of \$2,500,000 was made and \$5,250,000 of the second mortgage loan was applied to the purchase price. On possession of Phase II of the property on September 1, 2008, the balance of the second mortgage loan of \$4,750,000 was applied to the purchase price. After accounting for the payment of an additional deposit of \$2.5 Million on October 1, 2008, the balance owing on Parsons Landing was \$48.2 Million as of December 31, 2008, including GST.

The balance owing was due on February 28, 2009, with interest of \$1,077,594 from January 1, 2009 to February 28, 2009.

The mortgage financing for Parsons Landing has been delayed and, as a result, the vendor has agreed to extend the deadline for payment of the balance owing until May 29, 2009 with interest of \$2,621,175. The vendor has also agreed to accept partial payment on account of interest of \$600,000, payable in two installments of \$300,000 in March and April of 2009 and to reduce the balance by \$1.4 Million on payment at closing. The payment extension is conditional upon the Trust obtaining a commitment for mortgage financing of \$45,000,000 by April 15, 2009. In the event that a financing commitment is not received by April 15, 2009 or any other act of default, the vendor shall be permitted to list the property for sale.

In the event of the sale of Parsons Landing, the Trust will be liable to the vendor for any shortfall between the net proceeds of the sale and the acquisition cost payable of \$45,733,000 plus interest.

Mortgage Guarantee Fees

The Trust has outstanding commitments to pay mortgage guarantee fees to guarantors on certain of the mortgage loans payable until the mortgage terms are amended to remove the guarantors or the mortgages are refinanced.

Amounts due under the commitments are as follows:

Year ending December 31	
2009	\$ 170,329
2010	166,615
2011	162,668
2012	158,473
2013	124,013
Thereafter	<u>203,940</u>
	<u>\$ 986,038</u>

LANESBOROUGH REAL ESTATE INVESTMENT TRUST

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
DECEMBER 31, 2008 AND 2007**27 Commitments (continued)****Management Contracts**

The Trust has retained the following third party managers to provide on-site management services to the seniors housing complexes:

<u>Property</u>	<u>Manager</u>	<u>Term Expiring</u>
Riverside Terrace	LutherCare Communities	July 31, 2015
Chateau St. Michael's	Integrated Life Care Inc.	September 30, 2010
Elgin Lodge	Kingsway Arms Management Inc.	May 31, 2016
Clarington Seniors Residence	Kingsway Arms Management Inc.	February 12, 2017

In addition, Siena apartments condominium is managed by Pacer Management Inc. for a term expiring 2012.

28 Contingent consideration on acquisition**Elgin Lodge**

During the five year period from June 1, 2006, Kingsway Arms Management Services Inc. is entitled to a one-time payment equal to 50% of the amount by which the appraised value of the expanded Elgin Lodge property exceeds the total of the cost to the Trust, including the expansion costs and the unpaid portion of a 12% return on equity. Consideration recorded at December 31, 2008 of \$314,869 (2007 - \$194,756), which increases the cost of the building, is included in accounts payable and accrued liabilities.

Clarington Seniors Residence

During the five year period after lease-up is achieved, Kingsway Arms Management Services Inc. is entitled to a one-time payment equal to 50% of the amount by which the appraised value of the property exceeds the total of the acquisition cost to the Trust and the unpaid portion of an 8% return on equity. Consideration recorded at December 31, 2008 of \$313,951 (2007 - \$150,001), which increases the cost of properties under development, is included in accounts payable and accrued liabilities.

29 Subsequent events**Distributions**

Distributions of \$752,162 and \$778,583 were paid on February 15, 2009 and March 15, 2009 to unitholders of the Trust. Units of 23,439 and 25,137 were issued on February 15, 2009 and March 15, 2009 respectively, to unitholders of the Trust in regard to participation in the DRIP. Distributions of \$16,642 and \$16,642 were paid on February 15, 2009 and March 15, 2009 respectively, to the holder of the LP units of Village West LP.

Units cancelled

Subsequent to December 31, 2008, the Trust purchased and cancelled 99,507 units at a weighted average price of \$2.77, pursuant to terms of the normal course issuer bid.

30 Comparative figures

Certain of the prior year figures have been reclassified to be comparable to the current year.

UNITHOLDER INFORMATION

Trustees and Officers

The investment policies and operations of LREIT are subject to the control of the trustees, pursuant to the terms of a Declaration of Trust. The Declaration of Trust provides for a minimum of three trustees and a maximum of ten trustees and requires that the majority of trustees be independent trustees. The Declaration of Trust provides Shelter Canadian Properties Limited with the right to appoint one trustee.

The current trustees of LREIT are Mr. Charles Loewen, Mr. Earl Coleman, Mr. Harold Milavsky, FCA, Ms. Cheryl Barker, CA and Mr. Arni Thorsteinson, CFA. Mr. Loewen is the Chief Executive Officer of Online Enterprises Inc. and serves as Chairman of LREIT. Mr. Coleman is the President of Big Freight Systems Inc. Mr. Milavsky and Ms. Barker were appointed at the Annual General Meeting in June 2006. Mr. Milavsky is the Chair of the Board, Quantico Capital Corporation. Ms. Barker was the President, MTS (Manitoba) prior to her retirement in February 2006. Mr. Thorsteinson is the President of Shelter Canadian Properties Limited and serves as Chief Executive Officer of LREIT. Mr. Thorsteinson is the appointee of Shelter Canadian Properties Limited.

The Chief Financial Officer and Secretary of LREIT is Mr. Kenneth Dando, CA, Senior Manager of Corporate Accounting and Financial Reporting for Shelter Canadian Properties Limited.

Administrator of the Trust

Shelter Canadian Properties Limited has been appointed by the Trustees, pursuant to the terms of a Services Agreement, to administer the daily affairs of LREIT and to perform the accounting and reporting functions of LREIT.

Property Management

Shelter Canadian Properties Limited has been appointed by the Trustees, pursuant to the terms of the Property Management Agreement, to act as the Property Manager for all of the income properties in the LREIT portfolio. Shelter Canadian Properties Limited manages all of the income properties except for the Siena Apartments and the seniors housing complexes, where the Trust has retained third party property managers to provide on-site management services, due to the nature of the operations.

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Unit Listing

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Unit trading symbol: LRT.UN
Debenture trading symbol: LRT.DB.F
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